Coalition for Derivatives End-Users

June 6, 2011

Office of Financial Markets
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Submitted via Federal eRulemaking Portal, www.Regulations.gov

Re: *Determination of Foreign Exchange Swaps and Forwards under the Commodity Exchange Act, Notice of Proposed Determination 76 Fed. Reg. 25774 (May 5, 2011)*

The Coalition for Derivatives End-Users (the "Coalition"), which represents hundreds of companies that employ derivatives predominantly to manage risk, is pleased to respond to the Department of the Treasury's Notice of Proposed Determination announcing the Treasury's decision to exempt foreign exchange ("FX") swaps and forwards from the central clearing and trading requirements under the Commodity Exchange Act ("CEA") as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act").

The Coalition fully supports Treasury's determination, which recognizes the unique characteristics of the FX market and its strong performance during the financial crisis of 2008.[1] As Treasury noted in its Fact Sheet on the Proposed Determination, the FX market "already reflect[s] many of Dodd-Frank's objectives for reform—including high levels of transparency, effective risk management, and financial stability." We agree that the FX market is "markedly different from other derivatives markets," that the market helps "to mitigate risk and . . . ensure stability," and that imposing the panoply of regulations that will apply to the derivatives market on the FX market actually could jeopardize the market's current sound, risk-reducing practices. More specifically, we concur with the Treasury's assessment that (1) the FX swaps and forwards market already operate with higher levels of transparency; (2) FX swaps and forwards are unique when compared to other derivatives products; and (3) the FX market already is subject to strong, comprehensive oversight.

1. The FX market already operates with higher levels of transparency.

As the Coalition explained in its previous letter responding to Treasury's request for comments regarding a potential exemption for FX swaps and forwards, the FX market has pioneered the adoption of more transparent electronic trading platforms. Because the market is highly liquid

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[1] The Coalition submitted an in-depth analysis of the issues addressed by Treasury in its Request for Comment regarding the exemption for FX swaps and forwards on November 30, 2010, *available at*: http://www.regulations.gov/#!documentDetail;D=TREAS-DO-2010-0006-0031.

and decentralized, liquidity can exist more easily on multiple electronic platforms and pricing transparency is more readily available. Applying the clearing and exchange trading requirements to these transactions would not improve pricing transparency to any notable degree.

Moreover, business conduct requirements still apply to FX swaps and forwards. Even with the exemption from clearing and exchange trading, the Dodd-Frank Act still will require counterparties to report their FX transactions, which will allow the federal government to collect data on the FX market in a centralized location and to analyze it along with the rest of the swaps data it collects.

2. FX swaps and forwards are unique when compared to other derivatives products.

As noted in the Proposal and in the Coalition's previous letter, "unlike most other derivatives," FX swaps and forwards "have fixed payment obligations, are physically settled, and are predominantly short term instruments."[2] These features shift most of FX swaps and forwards' risk to the settlement process rather than to their counterparties. Counterparty credit risk is small in FX swap and forward contracts because the contracts are short in duration, and the FX market has addressed settlement risk already: the vast majority of FX swaps and forwards (90% of interdealer trades[3]) are settled through the CLS Bank.

Requiring FX swaps and forwards to be cleared and executed like other derivatives would introduce significant liquidity risks into the system where none have previously existed, deter prudent FX hedging and risk management, and encourage companies to move production abroad to create "natural hedges," harming U.S. economic growth.

3. The FX market already is subject to strong, comprehensive oversight.

During the 2008 crisis, the FX market's performance and oversight by the world's central banks remained remarkably stable. Almost all FX swaps and forwards occur between banks, as noted in the proposal,[4] which means that almost all the market's participants are subject to consolidated supervision. Furthermore, the G10 banking regulators coordinate their supervision to ensure international stability.

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[2] 76 Fed. Reg. 25774, 25776 (May 5, 2011).

[3] Commission of the European Communities, Staff Working Paper accompanying Commission Communication, Ensuring Efficient, Safe & Sound Derivatives Markets," at 41 [hereinafter EC Staff Working Paper] ("CLS is currently used for 55% of FX transactions (90% of the interbank market"))," available at http://ec.europa.eu/internal_market/financialmarkets/docs/derivatives/report_en.pdf.

[4] 76 Fed. Reg. 25774, 25777 (May 5, 2011).

The Notice of Proposed Determination states that the definition of foreign exchange swaps and forwards does not encompass non-deliverable forwards ("NDFs"). NDFs generally are utilized when practical problems exist with FX forwards, such as currency controls in the foreign country. NDFs are cash-settled, short-term forward contracts in a foreign currency, in which the profit or loss is calculated as the difference between the contractually agreed upon FX rate and the FX rate on the date of settlement. Similar to FX forwards, NDFs are used to hedge exposure to the FX markets and have a "fixed rate that is agreed upon on the inception of the contract."[5] When used to hedge a commercial risk in lieu of FX forwards, either because FX forwards are inaccessible or impractical, NDFs have an equivalent result as if FX forwards were used. Additionally, FX forwards, like NDFs, are oftentimes cash-settled because of the difficulty of predicting the timing of currency delivery. Given that NDFs are used for the same purposes and have the same effects on the market as FX forwards, we encourage the Treasury to work with other regulators and the Coalition to find authority to exempt NDFs from the central clearing and trading requirements for swaps under the CEA.

We thank Treasury for the opportunity to comment on these important issues. We also want to express our appreciation for the willingness of Treasury officials to meet with us in order to share perspectives on implementation of the derivatives title. The Coalition looks forward to working with Treasury to help implement rules that serve to strengthen the derivatives market without unduly burdening business end-users and the economy at large. We are available to meet with Treasury to discuss these issues in more detail.

Sincerely,

Business Roundtable
Financial Executives International
National Association of Corporate Treasurers
National Association of Manufacturers
National Association of Real Estate Investment Trusts
The Real Estate Roundtable
U.S. Chamber of Commerce

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[5] 7 U.S.C. 1a(24).