

# RIVERSIDE Risk Advisors

February 22, 2011

David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, NW  
Washington, DC 20581

Re: CFTC File: RIN 3038-AD25  
Implementation of Certain Provisions Related to the Business Conduct Standards For  
Swap Dealers and Major Swap Participants with Counterparties of Title VII of the Dodd-  
Frank Wall Street Reform and Consumer Protection Act

Dear Mr. Stawick:

We appreciate the opportunity to provide comments on proposed rules under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Act”) recently published by the Commodity Futures Trading Commission (the “CFTC”) governing the qualification of independent representatives under Section 4s(h)(5) of the Commodity Exchange Act.

Our firm, Riverside Risk Advisors LLC (“Riverside”) is an advisory boutique specializing in derivatives and structured financial products. We bring expertise and advice to our clients without conflicts of interest, resulting in transparency, better understanding of risks and improved pricing and transaction terms. Our professionals have extensive experience as derivatives structurers, traders and marketers at some of the world’s largest derivatives dealers. Our interest in providing commentary is in promoting the proper functioning of the derivatives markets by increasing access, transparency, innovation and sound decision-making, and not to serve the narrow interests of any particular constituency.

As the CFTC considers amendments and refinements to Title VII of the Act, we would like to ask it to consider the creation of a certification examination that an individual would be required to pass in order to serve as a qualified representative for purposes of Section 4s(h)(5).

## Background

Section 4s(h)(5) of the Commodity Exchange Act authorizes the CFTC to establish duties for Swap Dealers and Major Swap Participants that offer Swaps or enter into Swaps with Special Entities, including requiring a Swap Dealer or Major Swap Participant to have a reasonable basis to believe that the Special Entity has a representative, independent of the Swap Dealer or Major Swap Participant, that meets certain criteria, including having sufficient knowledge to evaluate the transaction and risks as well as undertaking a duty to act in the best interests of the Special Entity.<sup>1 2</sup>

## Our Proposal Regarding the Qualifications of Swap Advisors

We propose the creation of a certification examination (a “Swap Representative Certification”) that an individual would be required to pass in order to serve as a “qualified” representative for purposes of CEA Section 4s(h)(5).

Topics covered within a Swap Representative Certification examination would include the following:

- Mechanics of the products (swaps, options, caps and floors, futures, hybrids)
- Principles of valuation and replication
- Valuation models and adjustments
- Risk measurement and management
- ISDA Swaps documentation requirements, including definitions
- Exchange rules and OTC conventions
- Suitability issues
- Accounting and tax implications for Swaps
- Law and regulation of Swaps
- Swap Dealer and end-user best practices

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<sup>1</sup> Section 4s(h)(5)(A) of the Commodities and Exchange Act (“CEA”) provides that any Swap Dealer or Major Swap Participant that offers to enter or enters into a Swap with a Special Entity shall have a reasonable basis to believe that the Special Entity has an independent representative that:

- (I) has sufficient knowledge to evaluate the transaction and risks;
- (II) is not subject to a statutory disqualification;
- (III) is independent of the swap dealer or major swap participant;
- (IV) undertakes a duty to act in the best interests of the counterparty it represents;
- (V) makes appropriate disclosures;
- (VI) will provide written representations to the Special Entity regarding fair pricing and the appropriateness of the transaction; and
- (VII) in the case of employee benefit plans subject to the Employee Retirement Income Security Act of 1974, is a fiduciary as defined in section 3 of that Act (29 U.S.C. 1002).

<sup>2</sup> A parallel provision with respect to security-based swaps is contained in Section 15F(h)(5) of the Securities Exchange Act of 1934 (“1934 Act”). Our comments apply equally to the CEA and the 1934 Act.

Alternatively, should the CFTC choose not to impose a broad credentialing requirement, we propose the adoption of a safe harbor under which Swap Dealers and Major Swap Participants would be able to rely on the presence of an independent representative who has received a Swap Representative Certification to meet their obligations under CEA Section 4s(h)(5). This would be in lieu of some or all of seven factors listed under CEA Section 4s(h)(5)(A),<sup>3</sup> in particular with respect to the requirement that a representative “has sufficient knowledge to evaluate the transaction and risks.”

### Rationale

Properly constructed, such a credentialing process would promote the clear intent of this provision of the Act by bringing to Special Entities independent representation by professionals with expertise on par with the expertise of the Swap Dealer representatives with whom they transact.

It is clear that the existing certifications for securities, municipal securities, commodities and pension fund representatives do not cover the material one must master in order to provide expert Swap advice to Special Entities. The experience of some municipal entities relying on the services of under-qualified representatives holding themselves out as “swap advisors” illustrates the need for more rigorous and on-point credentialing.

We are aware of proposals by others to allow for a simple representation by the Special Entity in lieu of an assessment by the Swap Dealer as to the seven factors. While this would certainly ease burdens on dealers it would do little to improve the quality of representation. What municipal end-user, who in hindsight was poorly served by a purported “swap advisor,” would not have made a representation as to the advisor’s qualifications at the time? All too often, new or infrequent users are not in a good position to independently and objectively evaluate the quality of a swap advisor. A high bar, in the form of a credentialing process that tests the necessary skills and experience, can compensate.

It would benefit the market for Swap Dealers and Major Participants to have a clear, simple, and administrable means of demonstrating the requisite “reasonable basis” required under 4s(h)(5)(A). Having a Swap Representative Certification would be direct evidence of the “sufficient knowledge to evaluate the transaction and risks” involved.

### Conclusion

Properly constructed, a credentialing process such as a Swap Representative Certification would promote the clear intent of the “Special Entities” provision of the Act by providing Special

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<sup>3</sup> See footnote 1.

Entities independent representation by professionals with expertise equal to that of the Swap Dealer representatives with whom they transact and would also remove the concerns and burdens associated with Swap Dealers determining who qualifies as a competent independent representative in the absence of objective criteria.

We would be pleased to discuss our recommendations in more detail, or to suggest specific operative language, should the CFTC so desire. Thank you again for this opportunity to comment.

Respectfully submitted,

Frank Iacono  
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Riverside Risk Advisors LLC

cc: Elizabeth M. Murphy  
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