September 26, 2011

David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st St., NW
Washington, DC 20581

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F St., NE
Washington, DC 20549-1090

Re: Stable Value Contract Study
SEC File Number S7-32-11

Dear Mr. Stawick and Ms. Murphy:

I am writing today on behalf of the American Benefits Council with respect to (1) the study required by section 719(d) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") regarding stable value contracts and (2) the request for comment ("Request for Comment") issued by the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") in connection with such study.

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

Under the Dodd-Frank Act, the CFTC and the SEC (collectively referred to as the "Commissions") are to conduct a joint study to determine (1) whether stable value contracts fall within the definition of a swap[1] under the Dodd-Frank Act, and (2) if so, whether an exemption from such definition is appropriate and in the public interest. The Request for Comment was issued to obtain information needed to complete the study.

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[1] As noted in the Request for Comment, the determination of whether a stable value contract is a swap "also is relevant to a determination of whether [stable value contracts] fall within the definition of the term 'security-based swap.'"

The purpose of the Dodd-Frank Act was to establish more safeguards against systemic risks that could threaten economic stability following the financial crisis. Stable value contracts, however, did not contribute to the crisis. We believe that the study should be undertaken in that context.

This letter sets forth our views on the issues to be addressed in the study. As a plan sponsor organization, the Council wants to emphasize three points in this letter[2]:

- Stable value contracts are a critical component of our country's 401(k) and other defined contribution plans, and these products fulfilled their economic and contractual obligations throughout the crisis.
- The financial institutions that issue stable value contracts (as defined for purposes of the study) are already subject to significant regulatory oversight. Application of the swap regulatory regime to stable value contracts could make the applicable costs prohibitive, thus undercutting their value to participants and perhaps eliminating their viability.
- Congress did not evidence any intent to treat stable value contracts as swaps.

Stable Value Contracts.

Stable value contracts support an extremely popular, conservative investment option under qualified defined contribution plans, such as 401(k) plans. Such contracts are offered under approximately 43.2% of all 401(k) plans and currently represent approximately 12.6% of all 401(k) plan assets; money market funds by contrast only represent approximately 5.3% of all 401(k) plan assets.[3] In fact, we understand from our members that in many plans, the stable value fund is the largest single fund, particularly in mature plans with a large retiree population. The popularity of the stable value option is attributable to two key factors. First, principal is preserved under stable value contracts, which provides critical protection against the daily fluctuations that occur in the equity and bond markets. Second, compared to money market funds, stable value contracts can offer participants a higher yield based on fixed income securities with a longer term. This higher yield makes stable value contracts very appealing and valuable to participants.

The above features of stable value contracts have made them especially attractive (1) to risk-averse participants, such as retirees who have shorter investment horizons and cannot ride out fluctuations in the market, and (2) as a component of any portfolio, offering diversification for participants who have substantial exposure to the equity and/or bond markets. In fact, many retirees find stable value funds especially helpful because (1) the predictable and substantial income can be matched up with fixed monthly expenses, and (2)

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[2]Although the discussion below addresses questions 1, 2, 4, 6, 7, 8, 9, and 12 from the Request for Comment, this letter does not attempt to answer every question in the Request for Comment, but rather emphasizes the key issues for analysis under the study.

[3] See "Plan Asset Allocation, Account Balances, and Loan Activity in 2009", Investment Company Institute Research Perspective, Nov. 2010, Vol. 16, No. 3.

this type of investment is not available outside the plan context. Losing this secure source of funds to pay such expenses would be extremely disruptive for retirees.

There are five main types of products that are commonly viewed as stable value contracts. Economically, the benefits of the five types of products for participants are generally similar; the analysis of the different products under the Dodd-Frank Act is, however, very different, as discussed below. The five main types of products are:

- **Synthetic Wrap Contracts.** Under Synthetic Wrap Contract arrangements, a bank, insurance company, or other entity issues a contract to a defined contribution plan (such as a 401(k) plan or other employee benefit plan (collectively referred to as a "Plan")). The contract may (1) guarantee both principal and accumulated interest with respect to a pool of fixed income securities held by the Plan, providing the "book value" at which plan participants are allowed to transact within their Plans or (2) offer a guaranteed withdrawal benefit on Plan-held securities.
- **General Account Contracts.** Under a General Account Contract, an insurance company has a contractual obligation to pay principal and interest at a specified rate or on a specified basis, usually for a defined period of time. The contract is the Plan's asset, and the contractual obligation is supported by the insurance company's general account, which does not constitute Plan assets.
- **Separate Account Contracts.** These are generally the same as General Account Contracts except that the underlying assets are set aside in a separate account of the issuer to support the obligations under the contract.
- **Guaranteed Investment Contracts ("GICs").** Traditional GICs are group annuity contracts issued by insurance companies that guarantee stated interest and principal and are benefit-responsive, maintaining participant withdrawals at book value. The guarantee is backed by the insurance company's general account assets.
- **Synthetic GICs.** Synthetic GICs, also known as "security-backed GICs", are an investment consisting of a pool of assets owned directly by the Plan and a wrap contract issued by banks or life insurance companies providing book value protection for participant withdrawals prior to maturity.[4]

Do Stable Value Contracts Fall Within the Definition of a Swap?

Definition of Swap. The definition of a swap under the Dodd-Frank Act is understandably broad. For example, under section 1a(47)(A)(ii) of the Commodity Exchange Act ("CEA"):

[4] There are also stable value contracts issued by an insurance company or a bank used in conjunction with a variable life insurance product held by an employer to indirectly fund employee benefit obligations, which we believe should also be exempt from the definition of swap or security-based swap for the same reasons provided below.

> Except as provided in subparagraph (B), the term "swap" means any agreement, contract, or transaction—…
>
> (ii) that provides for any purchase, sale, payment, or delivery (other than a dividend on an equity security) that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or a contingency associated with a potential financial, economic, or commercial consequence….

This is only one part of the definition of a swap, but it serves very well as a means of focusing the discussion, since it presents a simple structure that could be read to sweep in stable value contracts, but was not intended to. Accordingly, this letter addresses stable value contracts in the context of this part of the swap definition as an illustration of how the entire definition should be interpreted.

The part of the definition quoted above is extremely broad. Read literally, a swap would include any payment that is dependent on a financial, economic, or commercial trigger (subject to the statutory exclusions). So, for example, read literally, all company bonus programs that are based on company performance would be swaps—and generally illegal swaps, since most employees are not eligible contract participants. Similarly, substantially all commission payments would be illegal, as would sales incentives. Literally, there are countless examples of benign everyday practices that would fall within the literal words of the definition. Obviously, Congress did not intend to ban substantially all company bonus programs, commissions, sales incentives, and hundreds of other everyday practices. On the contrary, Congress intended that the Commissions would interpret the definition of a swap in accordance with the intent of the legislation.

The definition goes on to exclude certain instruments from the definition of a swap. Specifically, the definition excludes "any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities, including any interest therein or based on the value thereof, that is subject to—(I) the Securities Act of 1933 (15 U.S.C. 77a et seq.); and (II) the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.)".

The stable value contract study raises a threshold definitional issue. During the legislative process, officials within Congress and the Administration repeatedly stated informally that they never intended stable value contracts to be swaps. However, they did not want to create an explicit exception for stable value contracts because they were concerned about the political precedent of doing so. A study was less worrisome from a precedent perspective. So this study effectively presents the Commissions with an opportunity to clarify that the language of the statute will not be read so broadly as to effectively eliminate access to a critical feature of Plans, contrary to any purpose underlying the Dodd-Frank Act.

Application of the definition of a swap to stable value contracts. In this context, the next step is to apply the definition of a swap to stable value contracts. General Account Contracts, Separate Account Contracts, and Traditional GICs clearly do not fall within even the broadest definition of a swap. Such contracts are simply standard insurance contract payment promises, i.e., promises to pay. Synthetic Wrap Contracts and Synthetic GICs (together referred to as "Synthetic Contracts"), on the other hand, could, on a very literal basis, fit within the first part of the above quoted language that defines a swap. Under a Synthetic Contract, a payment could be triggered by a financial contingency—generally, the liability of a Plan to make distributions at book value (i.e., distributions of principal and accumulated interest) from the Plan's stable value subaccount, in conditions specified by the contract.

However, we believe that the statutory exclusion for "any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities" should encompass Synthetic Contracts because these contracts are guarantees that the value of a portfolio of securities, which may be fixed at the inception of the contract or actively managed over the duration of the contract, does not fall below book value at maturity of the contract. That guarantee is a cash settled put option on a basket of securities. On maturity of the contract, the Synthetic Contract provider pays to the plan holder the excess, if any, of the book value of the portfolio over the fair market value of the assets in the portfolio. Therefore, we believe that Synthetic Contracts are economically equivalent to put options, which are excluded from the definition of a swap.

Congressional intent. The statutory requirement that the treatment of stable value contracts be studied reflects (1) Congress' perception that stable value contracts could possibly fall within the literal language of the statute (unless the exclusion for put options applies), and (2) Congress' concerns about the appropriateness of that result. If the Commissions do not conclude that Synthetic Contracts are excluded from the definition of a swap, an alternative is to treat Synthetic Contracts as swaps and then provide an exemption for such Contracts. For reasons discussed later in this letter, however, we believe that although that might be one workable result, it is not the preferred result for all parties. Stable value contracts have many characteristics that distinguish them from swaps.

In their proposed regulations regarding the definition of a swap, the Commissions recognized that the broad definition of a swap must be interpreted based on a common sense perception of Congressional intent. Despite the possibility that the broad definition of a swap could possibly be read to include insurance products, the Commissions very appropriately found that to be inconsistent with Congressional intent. The rationale for the Commissions' conclusion appears to be the following:

- Insurance companies are heavily regulated.

- There is no evidence that the Dodd-Frank Act intended to interfere with these existing regulatory systems.
- Insurance contracts have never been thought of as swaps, and in the absence of Congressional intent to treat them as such, the Commission did not propose to do so.

The same analysis applies to stable value contracts. By definition, all Synthetic Contracts that are subject to the study are issued by a "bank, insurance company, or other State or federally regulated financial institution." Thus, all Synthetic Contracts subject to the study are issued by a regulated entity. Moreover, there is no evidence that Congress intended to interfere with the existing regulatory system in light of the fact that stable value contracts have never been thought of as swaps.

In addition, the insurance exception in the Commissions' proposed swap definition supports our position. ("The Commissions do not interpret this clause[5] to mean that products historically treated as insurance products should be included within the swap or security-based swap definition.")[6] The proposed regulations defer to the Commissions' study, and do not explicitly address stable value contracts issued by insurance companies and regulated by insurance regulators; nevertheless, Synthetic Contracts issued by insurance companies could fit within the insurance exception, but that is not clear. What is clear, however, is that Synthetic Contracts would fit conceptually within each proposed component of the insurance product exception:

- The Plan has an insurable interest and a risk of loss, i.e., a decline in the value of the securities under conditions specified in the contract (see, e.g., Prop Reg. § 1.3(xxx)(4)(i)(A));
- In order to collect on the Synthetic Contract, the Plan must incur that loss and prove it (see, e.g., Prop Reg. § 1.3(xxx)(4)(i)(B));
- Synthetic Contracts are not traded on an organized market or over-the-counter, and, in fact cannot even be assigned (see, e.g., Prop. Reg. § 1.3(xxx)(4)(i)(C)); and
- Synthetic Contracts subject to the study are only provided by regulated companies (see, e.g., Prop Reg. § 1.3(xxx)(4)(ii)). Insurance companies and banking institutions are regulated entities. Likewise, defined contribution plans that acquire or participate in stable value funds are regulated by ERISA's fiduciary standard of care when entering into the contract and by significant disclosure rules. Governmental plans exempt from ERISA are subject to state laws that impose their own standards, which may be similar to ERISA.

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[5] See Federal Register, Vol. 76, No. 99, May 23, 2011 at 29821 ("the statutory definition of the term 'swap' includes, in part, any agreement, contract or transaction 'that provides for any purchase, sale, payment, or delivery (other than a dividend on an equity security) that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence'").

[6] Federal Register, Vol. 76, No. 99, May 23, 2011 at 29821.

Moreover, Synthetic Contracts are individually negotiated and subject to a careful underwriting process that takes into account the stable value fund's cash flow history, asset size, and investment guidelines applicable to the wrapped assets. Such contracts do not involve the type of systemic risk that Congress sought to address in the Dodd-Frank Act.

We would offer the following additional reasons why Synthetic Contracts are not swaps and should not be swaps:

- Synthetic Contracts by their nature are not leveraged. Every Synthetic Contract relates to a pool of Plan assets that rarely falls far below book value. For example, in the middle of the 2008 economic crisis, the market to book ratio for stable value contracts averaged 95%.[7]
- Synthetic Contracts are each unique and could not be subject to clearing.
- Treatment as a swap would, by reason of section 12(h) of the CEA, preclude state regulation of insurer-issued stable value contracts as insurance. This could actually preclude insurers from issuing Synthetic Wrap Contracts, which would have devastating effects on Plans and participants, potentially severely limiting the availability of stable value contracts, since there is already a very serious capacity issue with respect to stable value contracts. See, e.g., Department of Labor, Employee Benefits Security Administration, Advisory Council Report, Report on Stable Value Funds and Retirement Security in the Current Economic Conditions, 2010 (stating that the Council heard testimony from the Stable Value Investment Association ("SVIA") regarding concerns about shrinking capacity of stable value product issuers/providers); Stable value: Still relevant in DC Plans, Russell Investment, Jan. 2011(stating that the limited capacity in the stable value context has created higher fees); Vanguard, Stable Value: Navigating Past the 2008 Credit Crisis, March 2011 (stating the effects of the 2008 credit crisis include fewer high-quality issuers of stable value wrap contracts, and higher wrap fees).
- Unlike swaps, there is not a "market" in Synthetic Contracts. As noted, they are not traded on an organized market or over the counter. And there are no dealers that serve as both sellers and buyers.
- The fundamental trigger for payment under a Synthetic Contract is not the performance of the unwrapped assets, but rather the "uncoordinated" mass exodus of participants from the stable value fund at a time when the value of the wrapped assets is below book value. This is unlike any swap transaction.
- A Synthetic Contract involves restrictions on the investment of the wrapped assets, a feature not generally found in swaps.

Application of the swap regulatory regime would have severely negative effects on Synthetic Contracts. Additional regulation of Synthetic Contracts will not promote the objectives of the new regulatory framework for swaps. The value of stable value contracts lies in the fact that they can offer both principal protection and

[7] December 2008 Stable Value Funds Quarterly Characteristics Survey by the Stable Value Industry Association.

materially higher rates of return than money market funds to participants. If the swaps regulatory regime were to become applicable, the cost of providing a Synthetic Contract would increase substantially, thereby reducing the rate of return possibly to the point that the product is no longer viable. Moreover, this would directly hurt participants, because as noted there is already a very serious capacity issue in the stable value market.

The causes of the cost increases could include the following:

- The calculation and adjustment of daily margin amounts would be very costly and, as noted above, of very little value.
- The application of additional and overlapping margin or minimum capital requirements on entities already highly regulated would be burdensome, costly, and again unnecessary.
- Compliance with the elaborate swap reporting and recordkeeping rules that were never designated for these types of products, would produce mountains of questions, uncertainties, and costs.

In addition, if a Synthetic Contract were deemed to be a swap, then the issuer of the contract would be subject to, among other requirements, the business conduct standards applicable to "swap dealers" under Title VII of the Dodd-Frank Act. These business conduct standards impose a number of requirements on the issuer of the contract when dealing with an ERISA plan, and complying with those standards could result in the issuer becoming an "advisor" under Title VII and a "fiduciary" under ERISA. If the issuer owes a duty to act in the Plan's "best interests" (which is a requirement of advisors under Title VII) or is a fiduciary under ERISA, this will jeopardize the ability of the issuer to issue a Synthetic Contract to the plan for the reasons described in our prior comment letters on the business conduct requirements.

Conclusion

We urge the Commissions to clarify that stable value contracts are not swaps or security-based swaps for the reasons discussed above. If the Commissions nonetheless determine that Synthetic Contracts are swaps or security-based swaps at least under certain circumstances, we urge the Commissions to use their authority to exempt such Contracts from the definition of a swap or security-based swap, again for the reasons stated above. For the reasons set forth above, however, we strongly believe that stable value contracts are not swaps, and prefer that result to the exemption approach.

We fear that any treatment of stable value contracts as swaps could have consequences in other areas which could disregard exercises of exemptive authority. For example, it is certainly possible that current or future legislation or regulation at the Federal or State level could simply cross reference the definition of a swap in the Dodd-Frank Act. If the Commissions use their exemptive authority, there would be at the

least substantial uncertainty as to whether stable value contracts are picked up by such cross references. The 401(k) plans across the country and the participants they benefit do not need that type of uncertainty and the costs that flow from such uncertainty.

We ask the Commissions to follow Congressional intent and clarify that stable value contracts are not swaps or security-based swaps.

Thank you for your consideration of our views.

Sincerely,

Jan Jacobson
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