Европейска инвестиционна банка
Evropská investiční banka
Den Europæiske Investeringsbank
Europäische Investitionsbank
Euroopa Investeerimispank
Ευρωπαϊκή Τράπεζα Επενδύσεων
European Investment Bank
Banco Europeo de Inversiones
Banque européenne d'investissement
Banca europea per gli investimenti
Eiropas Investīciju banka
Europos investicijų bankas
Európai Beruházási Bank
Bank Ewropew tal-Investiment
Europese Investeringsbank
Europejski Bank Inwestycyjny
Banco Europeu de Investimento
Banca Europeană de Investiții
Európska investičná banka
Evropska investicijska banka
Euroopan investointipankki
Europeiska investeringsbanken

July 22, 2011 SG-JU/JU CORP/FI/2011-2186/RS/kf

David A. Stawick, Secretary
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, DC 20581

Elizabeth Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*
File No. S7-16-11; SEC Rel. No. 33-9204

Dear Mr. Stawick and Ms. Murphy:

The European Investment Bank (the "Bank") is pleased to submit this letter to the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") (together, the "Commissions") in response to the request for public comment with regard to proposed rules and interpretive guidance under the Commodity Exchange Act ("CEA") and the Securities Exchange Act of 1934 ("Exchange Act") to further define the terms "swap," "security-based swap," and "security-based swap agreement" (collectively, "Product Definitions"), regarding "mixed swaps," and governing books and records with respect to "security-based swap agreements."[1] For the reasons stated below, we respectfully request that final regulations adopted by the Commissions clearly provide that the definitions of "swap" and "security-based swap" exclude swaps and security-based swaps to which the Bank is a counterparty.

[1] *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, 76 Fed. Reg. 29818 (May 23, 2011) (hereinafter the "Release"). The proposed rules are issued pursuant to Section 712(d)(1) of the of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), which requires the Commissions, in consultation with the Board of Governors of the Federal Reserve (the "FRB") to provide further definitions of such terms as "swap" and "security-based swap." Accordingly, we are providing a copy of this letter to the FRB, as well as to other financial regulators who are in the process of formulating new regulations for swap transactions under the Dodd-Frank Act.

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I. The European Investment Bank.

A. Background.

The European Investment Bank is an autonomous public institution operating on a non-profit making basis, comparable with other development banks, such as the Asian Development Bank and the European Bank for Reconstruction and Development.

The Bank, owned entirely by the Member States of the European Union, is the financing institution of the European Union. It was created in 1958 under the original Treaty of Rome, and remains authorized under the Treaty on European Union and the Treaty on the Functioning of the European Union, amending the Treaty of Rome. It is constituted pursuant to the Statute of the European Investment Bank ("the Statute"). The Statute, as amended, is set out in a Protocol annexed to the Treaty on the Functioning of the European Union. As an annexed protocol, the Statute is an integral part of, and has the same legal force as, the Treaty.

The Bank's mission is to foster the balanced and steady development of a common market among Member States of the European Union. To that end the Bank focuses on co-financing projects by working with banks as well as corporate and public sector project promoters in the less-developed regions of the EU. To fulfill this purpose the Bank provides financing, in particular in the form of loans and guarantees for projects that foster economic cohesion and convergence, and in areas that include promotion of environmental sustainability and that provide support for sustainable, competitive and secure energy.

To a more limited extent, the Bank also provides funding for certain development projects outside the EU, accounting for approximately 10% of the Bank's portfolio. Most of the Bank's financing operations outside the Union are carried out under an EU budget guarantee, set out in the so called external mandates for the Bank's activities in the different regions of the world. In that context the Bank works in close cooperation with EU institutions, governments of EU and partner countries and other international or bilateral financing institutions. Activities outside the European Union are devoted to emerging economies, notably EU-candidate countries, neighboring countries such as Russia and other countries on the EU's eastern perimeter, Mediterranean partner countries, and Asian, African, Latin American, Caribbean and Pacific countries. Projects in these areas support development of private sector enterprises, the financial sector, infrastructure, secure energy supply and environmental sustainability.

B. Ownership, Governance and Financing Activity.

The Bank is owned entirely by the Member States of the European Union. The Member States subscribe to the Bank's capital. In principle, each member's share is based on its economic weight within the EU (as expressed by gross domestic product).

Pursuant to the Statute, the Bank is governed by a 27 member Board of Governors, each of whom is designated by a Member State of the EU. They are, primarily, the Finance Ministers of the EU Member States. The Board of Governors approves the overall strategy of the Bank, establishes credit policy guidelines, approves the annual account and balance sheet, decides on capital increases and approves activities outside the EU. The Board of Governors also appoints the 28 members to the Board of Directors on nomination by the Member States and the European Commission. The Board of Directors has sole power to make decisions on loans, guarantees and borrowings. It is also responsible for ensuring that the Bank operates within the parameters of the Treaty and the Statute. The Board of Governors appoints a Management Committee and a six-person Audit Committee. Thus, the EU Member States retain a high degree of oversight over the Bank's financial status and operations.

By Treaty and under its Statute, the Bank is to operate as a non-profit entity. Its mission is to finance sound projects (and not speculative activities), as stipulated in Article 309 (ex Article 267 TEC) of the Treaty on the Functioning of the European Union:

> The task of the European Investment Bank shall be to contribute, by having recourse to the capital market and utilising its own resources, to the balanced and steady development of the internal market in the interest of the Union. For this purpose the Bank shall, operating on a *non-profit-making basis*, grant loans and give guarantees which facilitate the financing of the following projects in all sectors of the economy: (a) projects for developing less-developed regions; (b) projects for modernising or converting undertakings or for developing fresh activities called for by the establishment or functioning of the internal market, where these projects are of such a size or nature that they cannot be entirely financed by the various means available in the individual Member States; (c) projects of common interest to several Member States which are of such a size or nature that they cannot be entirely financed by the various means available in the individual Member States (emphasis added).

In addition, pursuant to the Statute, the Bank's treasury activities are not oriented toward speculative trading or the pursuit of profit. In fact, as reflected in Art. 21 of the Statute "the *Bank shall not, in managing its investments, engage in any currency arbitrage* not directly required to carry out its lending operations or fulfill commitments arising out of loans raised or guarantees granted by it" (emphasis added).

Under its Statute, the Bank's lending volume is capped by a statutory gearing ratio. It is permitted to have outstanding loans of up to two and one-half times its subscribed capital, reserves, non-allocated provisions and profit and loss account surplus. The latter aggregate amount must be reduced by an amount equal to the amount subscribed (whether or not paid in) for any equity participation of the Bank.[2] As of December 31, 2010, the Bank's total subscribed capital was EUR 232,382,989,000, of which EUR 11,619,649,000 was paid-in, and reserves, non-allocated provisions and profit and loss account surplus totaled EUR 28,566,170,000.

C. The Bank's Funding.

The Bank raises capital for its financing operations primarily by issuing bonds on international capital markets. Bonds are issued in around 20 currencies, chief among them Euros, the US Dollar and British Pounds, in order to diversify and optimize funding sources. As an entity established by Treaty and due to its backing by 27 sovereigns in combination

[2] Statute Article 16, Section 5.

with its prudent and conservative risk and liquidity management policies, the Bank enjoys a AAA credit rating, which allows it to obtain favorable credit terms.

D Use of Swaps and Other Derivatives.

The Bank uses derivative instruments to hedge two main financial risks to which it is exposed, namely risks associated with changes in interest rates and foreign exchange rates. Indeed the Bank employs derivatives in order to hedge specific risks associated with its fund raising operations and with the maintenance of liquid funds in its treasury. While the majority of the Bank's hedging is for this purpose, EIB also uses swaps in the context of its broader asset and liability management, i.e. hedging residual risks on its balance sheet such as loans, investments and the margin component of expected interest payments not denominated in EUR.

All of the Bank's long-term derivative transactions are conducted in the contractual framework of appropriate ISDA Master Swap Agreements with Credit Support Annexes, which specify the conditions of exposure collateralization by the Bank's counterparties. Financial risk and ALM (asset and liability) policy guidelines specify collateral management rules, and establish detailed eligibility criteria for swap counterparties. Credit risk associated with derivatives is managed by selecting first-class counterparties, and trading with counterparties only under collateral agreements. Of the notional value of the Bank's derivatives portfolio, 96.4% was with counterparties that have a long term rating awarded by Moody's of A-1 or higher in 2010.

The Bank is forbidden from seeking to generate profit from OTC derivatives transactions. As noted above, the Statute provides that the Bank "*shall not, in managing its investments, engage in any currency arbitrage not directly required* to carry out its lending operations or fulfill commitments arising out of loans raised or guarantees granted by it."[3] (emphasis added).

II. Application of Proposed U.S. Regulations.

A.-Applying US Swaps Regulation to EIB Would Negatively Impact Pursuit of Its Public Mission.

As initially proposed, the regulations implementing Title VII of Dodd Frank do not distinguish between multilateral development entities such as EIB and private, commercial entities. Application of US regulation to international development banks, however, would reduce the effectiveness of these organizations and, in the case of the Bank, undermine the policies of the EU Member States that authorize and direct its activities.

The use of swaps and other over-the-counter derivatives by EIB is essential to reducing the risk and lowering the costs associated with its borrowing and lending operations. Indeed, the Bank would be unable to provide the current level of financing without its existing hedging strategies. The proposed swap regulations, if applied to the Bank's swaps, could significantly affect the Bank's ability to hedge in a cost-efficient manner.

[3] Statute, Article 21.

At present, as a triple-A rated supranational entity, the Bank is not required by law or any regulation to post collateral on its swap transactions, and as a commercial matter, it does not. Resources not posted as collateral are available to support development projects. However, under the proposed regulations, the Bank would likely be required to post both initial and variation margin with its counterparties for all uncleared swaps. In addition, EIB could be required to clear its trades through central counterparties and execute its swaps on exchanges or swap execution facilities. This would both reduce the Bank's hedging flexibility and increase its costs.

We recognize that both the CFTC and the SEC have proposed exemptions for certain commercial end users from margin requirements for uncleared swaps and from mandatory clearing and exchange trading. However, it is not clear whether such exemptions would be available to the Bank because, as the rules are now proposed, the Bank might be deemed a financial entity, which would disqualify it from the more flexible treatment that would be afforded to other end users.

It is also possible that the Bank might be deemed to be a major swap participant, or a major securities based swap participant. As such the Bank would be subject to US registration, capital and margin requirements, and reporting, recordkeeping, inspection and business conduct standards. Such regulatory treatment would be fundamentally inconsistent with principles of international comity governing the treatment of development banks owned by sovereign nations and subject to another, comprehensive regulatory scheme deemed adequate by those states.

Finally, we note that imposition of the proposed regulations--in addition to presenting a significant intrusion into the management and operations of a foreign sovereign-owned and operated entity-- would also be extraordinary in that the necessary approval for implementing the changes required by US regulation may require amendment of the Statute which in turn would require the consent of the European Council (heads of government) and consultation with the European Parliament.[4]

B. EIB's Use of Swaps Presents No Systemic Risk to the Financial System.

It is difficult to see how EIB's use of swaps to hedge its interest rate and currency risks presents a significant risk to the US financial system. The Bank derives strength from 27 sovereign states, and is governed by their finance officials. The strength of EIB's capital base is evidenced by subscribed capital and reserves (EUR 261bn) equal to 60% of the balance sheet.

Thus, the Bank is 0% risk-weighted under the rules of the Basel Committee on Banking Supervision (standardized approach)[5] and has a Triple-A credit rating from the three

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[4] Article 308 of the Treaty on the Functioning of the European Union.

[5] ANNEX VI of the 2006/48/EC Capital Requirements Directive:

STANDARDIZED APPROACH: Part 1, Risk weights

20. Exposures to the following multilateral development banks <u>shall be assigned a 0 % risk weight</u>:

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major rating agencies. The Bank's securities are also recognized as High Quality Liquid Assets (for calculation of the Liquidity Coverage Ratio) by the Basel Committee on Banking Supervision. EIB's swaps positions did not contribute in any way to the recent financial crisis. To the contrary, EIB was a source of strength and provided a vehicle through which the EU and its Member States could provide financing for projects to aid in the economic recovery.

On the other side of its swaps trades, the Bank operates with carefully chosen, highly rated counterparties that post significant collateral to cover both initial and variation margin requirements under the applicable ISDA Master Agreements and Credit Support Annexes. As a commercial matter, the EIB's counterparties would continue to post collateral notwithstanding any exemption the Commissions might grant for EIB derivatives.

III. Proposal.

The Bank supports the position expressed by the World Bank and the Bank for International Settlements in their letters to CFTC and SEC officials.[6] That is, the use of derivatives by the Bank and similar entities should continue to be authorized, monitored, and controlled by their sovereign members on a collective basis, rather than through national legislation and regulation. Thus, the Bank requests that the CFTC and SEC use their clear authority under section 712 of Dodd-Frank to exclude any agreement, contract, or transactions to which the Bank is a party from the definition of "swap" or "security-based swap".[7] This would permit the Bank to continue to pursue its valuable, public mission of

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(a) the International Bank for Reconstruction and Development;

(b) the International Finance Corporation;

(c) the Inter-American Development Bank;

(d) the Asian Development Bank;

(e) the African Development Bank;

(f) the Council of Europe Development Bank

(g) the Nordic Investment Bank;

(h) the Caribbean Development Bank;

(i) the European Bank for Reconstruction and Development;

(j) the European Investment Bank;

(k) the European Investment Fund; and

(l) the Multilateral Investment Guarantee Agency.

Official Journal of the European Union L.177/83 (June 30, 2006).

[6] World Bank Letter to Commissioner Jill Sommers, dated April 5, 2011; BIS letter to A. Radhakrishnan and J. Brigaglianio, dated March 18, 2011.

[7] Section 712(d)(1) directs the SEC and CFTC to "further define" the terms "swap" and "security based swap" "[n]otwithstanding any other provision of this title." This broad grant of authority is not subject to any other limitations in the DFA, and is consistent with the inherent authority of the agencies to create rules that focus the effect of regulations on persons and entities that are most appropriate for oversight. For example, the Securities and Exchange Commission has exempted the World Bank from requirements of the Investment Advisors Act of

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supporting the real economy as it has done since 1958, free from burdensome and potentially conflicting national regulation. Alternatively, U.S. regulators could create specific exemptions from the clearing and margin requirements for international development banks, or clarify that the Bank would qualify as a commercial, nonfinancial end user, although these partial exemptions would be far less optimal than a "carve out" from the definition of "swap" or "security based swap".

Collective governance models in use for development banks owned by sovereign nations have worked well in the past. Indeed, sovereign states have recognized that imposition of any one national regulatory regime would unduly hinder the functions of the entities that they themselves created. Thus, they have adopted specific legal provisions that create privileges, immunities and governance structures unique to such institutions. For example, the proposed European Market Infrastructure Regulation (EMIR), which has regulatory objectives similar to those of Title VII of the Dodd-Frank Act expressly excludes the Bank and other multilateral development banks such as the European Bank for Reconstruction and Development and the Asian Development Bank from its coverage.[8] Under Section 752 of the Dodd-Frank Act, the Commissions must coordinate with non-U.S. regulatory authorities for the establishment of consistent regulatory standards for swaps.[9] As a matter of comity, actions by U.S. financial regulators should be consistent with the laws of other jurisdictions that provide exemption from national regulation for government-owned multinational development entities, such as the Bank. Just as it would be inappropriate for European financial regulators to set capital or other requirements for U.S. entities that borrow in Europe (such as government-sponsored enterprises), so it would be inappropriate for U.S. regulators to impose obligations on the EIB.

IV. Conclusion.

There is no evidence that Congress contemplated the regulation of entities such as the Bank when it passed Title VII of the Act. Development banks have not been linked to the problems that enveloped the swaps markets during the recent financial crisis. In fact, the Bank and other development banks have functioned well for years without duplicative, national regulation, due to their nature as multilateral, sovereign-backed entities. Moreover, when the Board of Governors of an institution is composed of the Finance Ministers of 27

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1940 notwithstanding the absence of a specific legislative exemption for multilateral development banks. *See* Investment Adviser Act of 1940 Release No. 1971 of September 4, 2001, 2001 SEC LEXIS 1782.

[8] Council of the European Union, Doc. 13012/11, available at register.concilium.europa.eu/pdf/en/11/st13/st13012.en11.pdf, July 18, 2011 draft: "multilateral development banks listed in (...) Annex VI of Directive 2006/48/EC should be excluded from the scope of this Regulation in order to avoid limiting their power to perform their tasks of common interest."

[9] Section 752(a) of the Act provides that the Commissions should pursue international harmonization:

> *In order to promote effective and consistent global regulation of swaps and security-based swaps, the Commodity Futures Trading Commission, the Securities and Exchange Commission, and the prudential regulators ... as appropriate, shall consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation (including fees) of swaps, security-based swaps, swap entities, and security-based swap entities...*

sovereign governments, the benefit of oversight by one nation's regulators would probably be small. Accordingly, we respectfully urge the Commissions not to impose significant, new regulation on the operations of the Bank. Instead the EIB respectfully requests that the Commissions expressly exclude transactions entered into by the Bank from the definitions of "swap" and "security-based swap."

We thank you for this opportunity to comment. If you have any questions about the EIB or the impact of the proposed rules on its core mission, please communicate with Whitney Debevoise of Arnold & Porter LLP at (202) 942-5042 or Whitney.Debevoise@aporter.com or Dan Waldman at (202) 942-5804 or Dan.Waldman@aporter.com.

Respectfully submitted,

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Secretary General and General Counsel

B. de Mazières
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cc: Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System

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