



asset management group

May 17, 2017

Nancy Markowitz
Deputy Director, Market Review Branch
Division of Market Oversight
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: **Recommendations regarding Swap Execution Facilities**

Dear Ms. Markowitz:

The Securities Industry and Financial Markets Association's Asset Management Group ("SIFMA AMG" or "AMG")¹ writes to provide its updated recommendations to the Commodity Futures Trading Commission (the "**Commission**") on optimization of the Commission's Part 37 requirements for Swap Execution Facilities ("**SEF**") promulgated under the Commodity Exchange Act ("**CEA**").² We will continue to provide feedback on this issue through the Commission's request for input on simplifying rules (i.e., Project KISS), but provide this letter in the interim.

AMG strongly supports the Commission's prior and ongoing efforts to implement the G20 commitment to, where appropriate, require central execution of standardized, liquid OTC derivative contracts; however, as we have stated in prior letters and at Commission roundtables,³ AMG members believe that changes to Part 37 and certain designated contract market ("**DCM**") rules are needed to make central execution of swaps work efficiently for the market and market participants, including certain recommendations made by the Acting Chairman in his 2015 whitepaper, *Pro-Reform*

¹ SIFMA AMG brings the asset management community together to provide views on policy matters and to create industry best practices. SIFMA AMG's members represent U.S. and multinational asset management firms whose combined global assets under management exceed \$39 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

² 17 CFR Part 37.

³ See SIFMA AMG, Letter in Response to Commissioner J. Christopher Giancarlo's White Paper, *Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank*, at 6-7 (May 11, 2015), available at <http://www.sifma.org/comment-letters/2015/sifma-amg-submits-comments-to-the-cftc-in-response-to-commissioner-giancarlo-s-white-paper-and-in-regards-to-the-sef-regulatory-framework/> ("**AMG 2015 Whitepaper Comment Letter**"); SIFMA AMG, *Comment on the Division of Market Oversight's Public Roundtable Regarding the Made Available to Trade; Request for Further Relief from Trade Execution Requirements for Package Transactions* (Aug. 17, 2015), available at <http://www.sifma.org/comment-letters/2015/sifma-amg-submits-comments-to-the-cftc-on-made-available-to-trade-determinations/>. ("**AMG 2015 Roundtable Comment Letter**").

Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank:⁴ At the same time, certain protections and structural fairness must be maintained and strengthened.

In summary, AMG believes that the Commission should:

1. Expand permitted modes of swap execution for swaps mandated for trading on SEFs (“**Required Transactions**”) in order to provide for a less prescriptive, more principles-based approach that balances transparency, competition, and liquidity through a flexible set of rules; any means of execution that provides sufficient pre-trade price transparency and preserves competitive execution should be available.
2. Fix known and identified problems with the Made Available to Trade (“**MAT**”) standards without making the MAT standards synonymous with the clearing requirement standards; certain market conditions should be met in order to require central execution, separate and apart from market conditions needed to require central clearing.
3. Require adjustment of DCM rules that prevent efficient pricing between swaps markets and futures markets.
4. Maintain strong impartial access requirements and continue non-discriminatory eligibility criteria for any market participant to become a SEF member.
5. Codify existing no-action relief covering the “occur away” requirement for block transactions, the ability to correct operational or clerical errors for certain cleared SEF trades, and the simplification of post-trade confirmation protocol requirements.

We provide below specific details on each of these recommendations.

1. Expand Methods of Execution for Required Transactions

AMG believes that Commission Regulation § 37.9 takes an unnecessarily prescriptive approach in restricting modes of execution for Required Transactions to central limit order book (“**CLOB**”) or request-for-quote (“**RFQ**”) to 3 dealers. While AMG agrees with the Acting Chairman’s view that SEFs should be permitted to offer various flexible execution methods,⁵ AMG expects that such an expansion would be reviewed by the Commission to ensure that the methodologies comply with the Core Principles, provide sufficient pre-trade price transparency, and ensure SEFs continue to offer competitive execution. Indeed, CEA § 5h(e) makes clear the

⁴ See J. Christopher Giancarlo, Commissioner, *Pro-Reform Consideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank* (Jan. 29, 2015), available at <http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/sefwhitepaper012915.pdf> (“**SEF Whitepaper**”).

⁵ SEF Whitepaper at 25.

Congressional goal “to promote the trading of swaps on swap execution facilities and to promote pre-trade price transparency in the swaps market.”⁶

AMG anticipates that this review of new execution methodologies would occur through Commission review of SEF rulebook changes with market participant comments taken into consideration. As we will address by separate comment, we believe the Part 40 process for material rulebook changes should be more robust, increasing both Commission powers to revise proposed rulebook changes and ability of market participants to provide comment on material rule changes. AMG would, therefore, recommend that as new methods of execution are proposed by SEFs that market participants are given an opportunity to provide their feedback to the Commission, after which the Commission has the authority to revise or reject the proposed changes.

By expanding available methods of execution, SEFs will be better-situated to attract liquidity, adapt to future technological innovations, and generally promote central execution of swap trading. We believe that these changes will advance the regulatory goals and benefit market participants.

2. Establish Standards for Central Execution Mandate that Recognize Necessary Market Conditions

AMG believes that the universe of swaps that must be executed on SEFs should remain a subset of the universe of swaps mandated for central clearing. This reflects the fact that the necessary market conditions that make central clearing appropriate are different from the necessary market conditions that make central execution appropriate. As such, it is appropriate that there are different, additional standards that must be met for a swap to be subject to the SEF trading requirement than for a swap to be subject to the clearing requirement.

Congress recognized that mandating swaps for clearing required certain market conditions to be met. Among the factors that the Commission must consider in making a clearing determination, CEA § 5h(2)(D)(ii)(II) requires an assessment of “[t]he availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded.”

In this same vein, requiring central execution of certain mandatorily-cleared swaps on SEFs requires consideration of additional factors pertinent to the trading of such swaps. These factors include each of the six factors set forth in Regulation 37.10 and the additional factors proposed in AMG’s recommendations submitted after the Commission’s July 2015 Roundtable on Made Available to Trade and Package Transactions.⁷ We refer you to this prior AMG submission,

⁶ 7 U.S.C. § 7b-3(e).

⁷ See SIFMA AMG, *Comment on the Division of Market Oversight’s Public Roundtable Regarding the Made Available to Trade; Request for Further Relief from Trade Execution Requirements for Package Transactions* (Aug. 17, 2015), available at <http://www.sifma.org/comment-letters/2015/sifma-amg-submits-comments-to-the-cftc-on-made-available-to-trade-determinations/>.

enclosed for your reference as reflecting AMG's current recommendations. We note that our prior submission also reflects our current views on how package transactions should be addressed.

3. Require Correction of CME Rule 538 and ICE Rule 4.06 to allow Exchange for Related Positions of Mandated Swaps

CME Rule 538⁸ and ICE Rule 4.06⁹ result in a *de facto* prohibition of exchange for related position (“**EFRP**”) transactions involving any Required Transaction, impairing the functioning of swaps markets.¹⁰ Under CME Rule 538, “[a] swap that is traded on, or subject to the rules of, a designated contract market (“DCM”) or a swap execution facility (“SEF”) is ineligible to be the related position component of an EFR or EOO transaction executed pursuant to Rule 538.”¹¹ In combination with the prohibition on executing Required Transactions off-facility, CME Rule 538 (and ICE’s similar rule) prohibit Required Transactions from being used in an EFRP. This conflict thwarts efficient pricing of markets in the same asset classes, putting at risk price correlation between the futures contracts and outright swaps trading on SEF. As such, AMG believes that CME and ICE Rules should be modified to permit EFRPs involving Required Transactions even when the swap is traded on or subject to the rules of a SEF. We believe that the Commission should direct these changes through its powers to oversee SEFs, including its authority to require compliance with core principles.

4. Maintain Strong Impartial Access Standards

Clear statutory language establishes impartial access as an important requirement for SEFs. Under CEA § 5h(f)(2)(B), each SEF is required to establish “means to provide market participants with impartial access to the market.”¹² This statutory mandate of impartial access is important to retail investment funds (e.g., mutual funds), pension funds and other clients served by asset managers. The ability of asset managers to hedge risks and achieve directional exposures through swaps depends on their ability to access deep, liquid, and competitive markets at the best price available for their clients. By including impartial access as a core principle for SEFs, Congress sought to promote a transparent and competitive OTC market landscape where participants could vie for

⁸ CME Group, Market Regulation Advisory Notice, RA1612-5, Rule 538 Exchange for Related Positions (Sept. 20, 2016), available at <http://www.cmegroup.com/rulebook/files/ra1311-5rr-rule538.pdf?redirect=/rulebook/files/ra1311-5r.pdf>.

⁹ ICE Futures U.S., Inc., Trading Rules, Rule 4.06 Exchange for Related Positions, available at https://www.theice.com/publicdocs/rulebooks/futures_us/4_Trading.pdf.

¹⁰ See AMG’s prior submissions on this issue, including: AMG 2015 Roundtable Letter at 7-9; AMG 2015 Whitepaper Letter at 13.

¹¹ CME Group, Market Regulation Advisory Notice, RA1612-5, Rule 538 Exchange for Related Positions (Sept. 20, 2016), available at <http://www.cmegroup.com/rulebook/files/ra1311-5rr-rule538.pdf?redirect=/rulebook/files/ra1311-5r.pdf>

¹² 7 U.S.C. § 7b-3(f)(2)(B)(i).

business based on price, services, and other commercial factors for the benefit of all market participants.

The Commission previously interpreted impartial access under this statutory mandate to require non-discriminatory access to SEFs for all market participants, irrespective of whether the market participant was a dealer or not. Specifically, the Commission, in its final rulemaking on the Core Principles and Other Requirements for Swap Execution Facilities¹³ in explaining the “requirements that SEFs provide market participants with impartial access to the market and that SEFs adopt and enforce rules with respect to any limitations placed on access to the SEF,” stated that “[t]he statutory language of Core Principle 2 requires that SEFs establish and enforce participation rules, including means to provide market participants with impartial access to the market, and that SEFs adopt and enforce rules with respect to any limitation they place on access.”¹⁴ The Commission further reiterated that:

[T]he purpose of the impartial access requirements is to **prevent a SEF’s owners and operators from using discriminatory access requirements** as competitive tool against certain ECPs or ISVs. ... [T]he impartial access requirement allows ECPs to **compete on a level playing field, and that the participation of additional liquidity providers will improve the pricing and efficiency of the market and reduce systemic risk**. As such, the Commission believes that access to a SEF should be determined, for example, based on a SEF’s impartial evaluation of an applicant’s disciplinary history and financial and operational soundness against objective, pre-established criteria.¹⁵

Importantly, the Commission interpreted the intended meaning of the term “impartial” in the CEA as “the **ordinary sense of the word**: fair, unbiased, and unprejudiced. Subject to these requirements, a **SEF may use its own reasonable discretion to determine its access criteria**, provided that the criteria are **impartial, transparent** and **applied in a fair and non-discriminatory manner**, and are not anti-competitive.”¹⁶

AMG believes that access to SEFs should remain open to all participants who satisfy non-discriminatory standards. While AMG agrees with Chairman Giancarlo’s observation that “Congress knew that there were D2C and D2D swaps markets before the Dodd-Frank Act, just as there are in many other mature financial markets,”¹⁷ the inclusion of the impartial access

¹³ 17 CFR Part 37, CFTC Final Rule, Core Principles and Other Requirements for Swap Execution Facilities, *available* *at*
<http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/federalregister051613b.pdf>.

¹⁴ *Id.* at 121.

¹⁵ *Id.*

¹⁶ *Id.* at 122.

¹⁷ SEF Whitepaper at 32.

requirement makes clear that mandating contracts for central execution impacts this prior market structure. If a contract must be executed on a SEF, market participants should not be discriminated against in seeking to access on-facility liquidity. AMG therefore strongly believes that impartial access is an important feature of the current market structure, and this feature should remain in place to provide investors with the best available pricing.

5. Codify Certain No-Action Letters Covering SEF Transactions

Alongside the recommended adjustments to the SEF rules, AMG believes that the Commission should codify existing adjustments that have been made successfully through no-action letters. These adjustments include:

- removing the “occurs away” requirement for block trades;¹⁸
- providing a mechanism to correct operational or clerical errors for certain cleared swaps executed on SEFs;¹⁹ and
- eliminating certain confirmation and post-trade recordkeeping related requirements for uncleared swaps executed on SEFs.²⁰

AMG believes that codification of this relief will streamline and simplify compliance with Part 37 requirements.

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We appreciate the opportunity to provide the Commission with our comments and are available to discuss our comments or any of the issues raised. Please do not hesitate to contact Tim Cameron at 202-962-7447 or tcameron@sifma.org or Laura Martin at 212-313-1176 or lmartin@sifma.org.

Respectfully submitted,



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¹⁸ CFTC Letter No. 16-74 (Oct. 7, 2016), *available at* <http://www.cftc.gov/idc/groups/public/@lrllettergeneral/documents/letter/16-74.pdf>.

¹⁹ CFTC Letter No. 16-58 (June 10, 2016), *available at* <http://www.cftc.gov/idc/groups/public/@lrllettergeneral/documents/letter/16-58.pdf>.

²⁰ CFTC Letter No. 17-17 (Mar. 24, 2017), *available at* <http://www.cftc.gov/idc/groups/public/@lrllettergeneral/documents/letter/17-17.pdf>