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asset management group

17 C.F.R. Part 43

July 25, 2013

Mr. Richard Shilts
Director, Division of Market Oversight
Commodity Futures Trading Commission
1155 21st Street NW Three Lafayette Centre Washington, DC 20581

Re: **Request for Relief Relating to Aggregation Provision in Final Block Trade Rule**

Dear Mr. Shilts:

The Asset Management Group (the "**AMG**")[1] of the Securities Industry and Financial Markets Association ("**SIFMA**") is writing to express its concerns relating to the prohibition on aggregating orders of different accounts for purposes of satisfying the minimum block trade size or cap size requirement contained in Rule 43.6(h)(6) (the "**Aggregation Provision**") under the Commodity Futures Trading Commission's (the "**Commission's**") recently adopted block trade rule.[2] Specifically, the AMG believes that asset managers should not be prohibited from aggregating client orders involving large notional off-facility swaps under the Aggregation Provision if the asset manager otherwise meets the conditions of the exception contained in clauses (i) and (ii) of Rule 43.6(h)(6) (i.e., exclusive of the requirement that aggregation be "on a designated contract market or swap execution facility"). Accordingly, we hereby request no-action relief or an alternative form of relief or clarification under regulation 140.99 to allow for large notional off-facility swaps to be included in the exception contained in the Aggregation Provision (the "**Investment Adviser Exception**"), or, alternatively, to be excluded entirely from the Aggregation Provision. We believe that it is essential that the Division of Market Oversight ("**Division**") promptly issue this relief as the Investment Adviser Exception appears to only allow aggregation for transactions subject to the rules of a designated contract market ("**DCM**") or a swap execution facility ("**SEF**"); while the Block Trade Rule will go into effect on July 30, 2013, swaps will not be listed or made available for execution on SEFs for several months after that date.

[1] The AMG's members represent U.S. asset management firms whose combined assets under management exceed $20 trillion. The clients of AMG member firms include, among others, registered investment companies, ERISA plans and state and local government pension funds, many of whom invest in commodity futures, options, and swaps as part of their respective investment strategies.

[2] 17 C.F.R. 43.6(h)(6). See Procedures To Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades, 78 Fed. Reg. 32,866, 32,940 (May 31, 2013) (the "**Block Trade Rule**").

On July 27, 2012, the AMG provided comments[3] to the Commission relating to its Proposed Rulemaking Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades.[4] In the 2012 AMG Comment Letter, we asked the Commission to clarify that the proposed aggregation prohibition applies solely to block trades. The AMG asked for this clarification because the language in the proposed aggregation prohibition referenced "minimum *block trade* size" (emphasis added), which is not a defined term and would seem to include only block trades by the incorporation of that term.[5] The Commission did not change the wording of the Aggregation Provision from the Proposed Rule and, although it is still not clear from the language of Rule 43.6(h)(6) itself, in the preamble to the Block Trade Rule, the Commission stated that it intends to include large notional off-facility swaps in the aggregation prohibition.[6] However, it remains unclear whether the Investment Adviser Exception also applies to large notional off-facility swaps.[7]

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[3] Comment Letter on the Proposed Rulemaking Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades (RIN 3038-AD84), SIFMA AMG (July 27, 2012), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=58342&SearchText= (the "**2012 AMG Comment Letter**").

[4] 77 Fed. Reg. 38,229 (June 27, 2012), available at http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-15481a.pdf (the "**Proposed Rule**").

[5] CFTC regulation 43.2 defines "block trade" to mean "a publicly reportable swap transaction that: (1) Involves a swap that is listed on a registered swap execution facility or designated contract market; (2) Occurs away from the registered swap execution facility's or designated contract market's trading system or platform and is executed pursuant to the registered swap execution facility's or designated contract market's rules and procedures; (3) Has a notional or principal amount at or above the appropriate minimum block size applicable to such swap; and (4) Is reported subject to the rules and procedures of the registered swap execution facility or designated contract market and the rules described in this part, including the appropriate time delay requirements set forth in § 43.5 of this [Part 43]." 17 C.F.R. 43.2. We also note that the Commission could have used the defined term, "appropriate minimum block size" in the proposed aggregation prohibition or in the Final Aggregation Prohibition, but declined to do so. "Appropriate minimum block size" is defined in CFTC regulation 43.2 as "the minimum notional or principal amount for a category of swaps that qualifies a swap within such category as a block trade or large notional off-facility swap," which includes both block trades and large notional off-facility swaps. Furthermore, the Commission referred to block trades, and not large notional off-facility swaps, in describing the proposed aggregation prohibition in the preamble of the adopting release of the Proposed Rule.

[6] As we stated in the 2012 AMG Comment Letter, we did not believe that the Aggregation Provision applied to large notional off-facility swaps and, given the ambiguities in the Proposed Rule, it was not until the release of the Block Trade Rule that we understood that the Commission was interpreting the aggregation prohibition to apply to both block trades and large notional off-facility swaps. Accordingly, we question whether there was sufficient opportunity for market participants to prepare for, and comment on, the inclusion of large notional off-facility swaps in the aggregation prohibition.

[7] CFTC regulation 43.2 defines "large notional off-facility swap" to mean "an off-facility swap that has a notional or principal amount at or above the appropriate minimum block size applicable to such publicly reportable swap transaction and is not a block trade as defined in § 43.2 of the Commission's regulations. 17 C.F.R. 43.2.

The AMG contends that, if the Commission intends to apply the aggregation prohibition to both block trades and large notional off-facility swaps, the Investment Adviser Exception to that prohibition should apply equally to both block trades and large notional off-facility swaps. We understand that the Aggregation Provision is generally meant to prohibit market participants from aggregating unrelated orders simply to obtain the benefits of block trades, including delayed public dissemination and cap size treatment. We also appreciate that the Investment Adviser Exception was adopted in recognition of the fact that qualified investment advisers have fiduciary responsibilities and bona fide business reasons for aggregating orders for different accounts. However, we have found no guidance on why large notional off-facility swaps and block trades would warrant different treatment for purposes of the Investment Adviser Exception. Both trades may be executed off of a SEF or DCM, but still ultimately be reported to a swap data repository. We believe that equivalent treatment of block trades and large notional off-facility swaps for these purposes is consistent with the Commission's rationale for establishing the Investment Adviser Exception.

In particular, investment advisers possess the same qualifications, and must comply with the same fiduciary duties towards their clients, regardless of whether a large swap trade is executed as a block trade or a large notional off-facility swap. Our members often aggregate client positions in large orders in order to seek the best possible price and overall terms for their clients' swaps transactions, consistent with their fiduciary duties as investment advisers, without signaling information to the market about their clients' positions or trading strategies. Our members must comply with the same fiduciary duties towards their clients, whether or not the swap in question is listed on, or executed pursuant to the rules of, a SEF or DCM. Not extending the Investment Adviser Exception to large notional off-facility swaps would be failing to recognize investment advisers' fiduciary responsibilities for all trades, as well as the established market practice of aggregating orders.

In addition, as the Commission has recognized in its Part 43 real-time reporting rules, it is important for large swap trades to enjoy the benefit of delayed reporting in order to allow dealer counterparties adequate time to hedge their exposure, irrespective of whether a swap trade is considered a block trade or a large notional off-facility swap. We believe that there is no market benefit to require block trades or large notional off-facility swaps to be subject to real-time reporting as these trades are frequently quoted or executed at off-market prices that do not reflect the price at which smaller trades can be executed. As we have pointed out in prior comment letters, not providing sufficient time to hedge large swap positions prior to public dissemination will result in a "winner's curse" whereby other market participants may be able to front-run the trade, leading to wider spreads on the client-facing trade, greater volatility and diminished liquidity.[8] Without the ability to utilize the real-time reporting delay and cap size limits for aggregated large notional off-facility swap orders, asset managers may break up these swaps into smaller trades in order to protect their global footprint, leading to increased transaction cost and

[8] See, e.g., Comment Letter on Procedures to Establish Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades (RIN 3038-AD08), SIFMA AMG (May 14, 2012), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=58193&SearchText=.

fees, the possibility of greater operational errors and heightened market inefficiencies. On the other hand, we find no perceivable benefit in not extending these precautions to large notional off-facility swaps. Indeed, it may be even more essential for large notional off-facility swaps that are not listed on SEFs or DCMs to be eligible for delayed public dissemination and capped notional amounts as these swap trades may be illiquid and/or bespoke transactions that require their counterparties to have more time to hedge their exposure. In addition, given the illiquidity or bespoke nature of these trades, there is greater risk that a swap counterparty will be identified, and therefore, greater need for utilizing cap size limits. Market participants should not be deprived from the benefits of these risk mitigants for swaps that have not been listed by any SEF or DCM. In fact, refusing to allow large notional off-facility swaps to be included in the Investment Adviser Exception removes the benefits of delayed public dissemination and cap size treatment from the parties that these provisions were designed to most protect.

We think it is imperative that the Division act on this request prior to July 30, 2013, when the Block Trade Rule goes into effect. Specifically, swaps will not be listed or capable of being executed on SEFs on July 30, 2013, and may not be for several months thereafter. Furthermore, no DCMs currently list swaps for trading. Yet the Investment Adviser Exception can only be used for aggregation "on a designated contract market or swap execution facility." Accordingly, if the language of the Investment Adviser Exception is to be read on its face, no investment advisers will be able to utilize the Investment Adviser Exception to aggregate their clients' swap trades immediately after July 30, 2013, as there will be no swap trades that are executed on SEFs or DCMs, and all swap trades that exceed the minimum block size will be deemed large notional off-facility swaps. In the long term, any swaps that are not listed on, or executed pursuant to the rules of, a DCM or SEF and that are entered into on an aggregated basis would be ineligible for a delay in public dissemination, resulting in harm to our members' clients as described above.

Requested Relief: For the reasons stated herein, we hereby request that the Division issue no-action relief or an alternative form of relief or clarification under regulation 140.99, to allow for large notional off-facility swaps to be included in the Investment Adviser Exception, or, alternatively, to be excluded entirely from the Aggregation Provision. Pursuant to regulation 140.99(c)(7), the AMG also asks that if no-action relief under this request is denied in whole or in part, the Commission staff consider granting alternative relief, under the facts and circumstances described in this request.

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Based on the foregoing, we respectfully request that the Division grant the relief described in this letter. We appreciate your consideration of this request, and stand ready to provide any additional information or assistance that the Division might find useful. Should you have any questions, please do not hesitate to contact Tim Cameron at 212-313-1389 or Matt Nevins at 212-313-1176.

Sincerely,

Timothy W. Cameron, Esq.
Managing Director, Asset Management Group
Securities Industry and Financial Markets Association

Matthew J. Nevins, Esq.
Managing Director and Associate General Counsel, Asset Management Group
Securities Industry and Financial Markets Association

cc: Hon. Gary Gensler, Chairman, Commodity Futures Trading Commission
Hon. Bart Chilton, Commissioner, Commodity Futures Trading Commission
Hon. Scott O'Malia, Commissioner, Commodity Futures Trading Commission
Hon. Mark Wetjen, Commissioner, Commodity Futures Trading Commission
John Dunfee, Assistant General Counsel, Office of the General Counsel, Commodity Futures Trading Commission
Ryne Miller, Counsel to Chairman, Commodity Futures Trading Commission
Megan Wallace, Counsel to Chairman, Commodity Futures Trading Commission

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Certification Pursuant to Commission Regulation 140.99(c)(3)

As required by Commission Regulation 140.99(c)(3), we hereby (i) certify that the material facts set forth in the attached letter dated July 25, 2013 are true and complete to the best of our knowledge; and (ii) undertake to advise the Commission, prior to the issuance of a response thereto, if any material representation contained therein ceases to be true and complete.

Sincerely,

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Timothy W. Cameron, Esq.
Managing Director, Asset Management Group
Securities Industry and Financial Markets Association

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Matthew J. Nevins, Esq.
Managing Director and Associate General Counsel, Asset Management Group
Securities Industry and Financial Markets Association