March 25, 2019

Mr. Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Post-Trade Name Give-Up on Swap Execution Facilities; Request for Comment – RIN 3038-AE79, 83 Fed. Reg. 61751 (Nov. 30, 2018)

Dear Mr. Kirkpatrick:

The Securities Industry and Financial Markets Association ("**SIFMA**")[1] welcomes the opportunity to provide the Commodity Futures Trading Commission (the "**Commission**") with comments on the above request for comment (the "**Comment Request**") relating to post-trade name give-up ("**PTNGU**") on swap execution facilities ("**SEFs**"). Although the views among our swap dealer members on PTNGU are not uniform, a majority of those who have expressed a view believe that PTNGU is important to the market and that its prohibition may impair participants' abilities to manage risk and provide liquidity. These members additionally do not believe there is sufficient evidence to support intervention by the Commission to prohibit PTNGU. The views of those members regarding this important topic are set forth below.[2] We believe that the matters for consideration present significant issues for the market as a whole and any decision should be made only after review of the important issues at play for all market participants.

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1 SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

2 We understand that views among SIFMA members who support prohibiting PTNGU will be expressed in other letters responding to the Comment Request, and so we are not addressing those views in this letter.

Introduction

PTNGU developed organically in the swaps market as an effective tool to promote liquidity provision. Meanwhile, SEFs can, and multiple SEFs do, offer anonymous trade matching without PTNGU. Market participants are thus free to choose for themselves as to whether it is in their independent interests to transact anonymously with or without PTNGU.

Prohibiting PTNGU would narrow the options available to market participants trading in swaps subject to the trade execution requirement, forcing them to choose between fully anonymous order books and fully disclosed request-for-quote methods of execution. The Dodd-Frank Act does not compel the Commission to engage in this picking and choosing among execution models, nor does it direct the Commission to drive the swaps market toward all-to-all anonymous trading. The Commission accordingly should not prohibit PTNGU nor any other market practice without considering its impact on all market participants—especially considering that available evidence shows that the current market structure has, overall, benefitted market participants through tighter pricing and increasingly deep liquidity.[3]

Further, continuing to permit PTNGU would be consistent with the Commission's proposal, in the release accompanying the Comment Request (the "**SEF Proposal**"),[4] to expand the ability of SEFs to offer different execution methods. Free markets, not the Commission, should determine what trading models are available to market participants.

Discussion

Permitting Diverse Trading Models Supports the Commission's Goals

The Commission should aim to preserve the diversity of trading models, which supports the Commission's goal of promoting SEF trading across a diverse range of products. Fully anonymous trading models are most closely associated with markets catering to a model of agency liquidity providers and to products that are generally small in size, frequently traded, highly liquid, and standardized, such as futures contracts. Most swap markets, including those whose products are subject to the trade execution requirement, do not exhibit these characteristics. Instead, they are based on liquidity providers trading as principal. In this regard, we agree with Chairman Giancarlo that "liquidity in the swaps

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3 *See, e.g.*, Lynn Riggs (CFTC), Esen Onur (CFTC), David Reiffen (CFTC) & Haoxiang Zhu (MIT, NBER, and CFTC), *Swap Trading after Dodd-Frank: Evidence from Index CDS* (Jan. 26, 2018) ("Riggs, Onur, Reiffen and Zhu") at p. 50 ("SEF-traded index CDS market seems to be working well after Dodd-Frank—dealers' response rates are high, the vast majority of customer orders result in trades, and customers' transaction costs are low"); and Pierre Collin-Dufresne, Benjamin Junge & Anders B. Trolle, *Market Structure and Transaction Costs of Index CDSs* (Sept. 12, 2017) ("Collin-Dufrense, Junge and Trolle") ("D2C prices are typically better than those available on the main interdealer limit order book, suggesting that clients who value immediacy could not get better execution by trading in the interdealer market.").

4 *See* [SEFs] and Trade Execution Requirement; Proposed Rule, 83 Fed. Reg. 61946 (Nov. 30, 2018).

market is fundamentally different than liquidity in futures and equities markets"[5] and makes use of execution methods that "[differ] markedly from the generally all-to-all market structure of the U.S. futures markets . . . ."[6] Given these differences, not every product can be, nor should be, traded fully anonymously. Attempting to force a market structure on a group of products and/or participants by fiat may be detrimental to pricing and liquidity.

In other products where traditionally over-the-counter markets have evolved to include fully anonymous trading models (*e.g.*, Treasuries, foreign exchange), such evolution occurred naturally, without regulatory intervention. SEFs are permitted to offer such models and, as for-profit entities, they are incentivized to develop and offer any permissible trading models that meet their participants' demands. In fact, some SEFs currently offer fully anonymous order books without PTNGU on a "dealer-to-client" ("**D2C**") basis, but participation in these order books has been very limited.[7] These preferences from market participants should be evidence that fully anonymous trading models are currently undesirable for swaps, at least for a substantial cross-segment of market participants. Prohibiting PTNGU would also risk diminishing the liquidity available on "inter-dealer" ("**D2D**") SEFs where it exists today. These D2D SEFs have attracted liquidity from dealer participants who use these platforms as a means to hedge their client activity. These participants may be unwilling or unable to continue to do so without PTNGU, as fully anonymous environments present conditions under which, as the CFTC noted has been a concern in its request, traders can more successfully "game the market" at the expense of other participants.[8]

Additionally, a key aspect of the SEF Proposal is to provide more flexibility to the market around the methods of execution for swaps that are subject to the trade execution requirement. The SEF Proposal also aims to simplify the requirements for the operation of a SEF so that, among other things, SEFs can allocate their resources to developing novel methods of execution. Anonymous trade matching with PTNGU is a method of execution distinct from others such as anonymous trade matching without PTNGU, request-for-quote, etc. By prohibiting a method of execution that is an adopted market practice, the Commission would not only be contradicting its overarching principle under the SEF Proposal about providing more flexibility to the trade execution regime, but it would also be discouraging SEFs from allocating resources to developing new methods of execution—as doing so would risk prohibition and a wasting of those development resources. Prohibiting a market practice because certain participants elect not to use one method of execution is not only an unfair result for those who elect to do so, but also a deterrent for SEFs and the market to develop new market practices.

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5 J. Christopher Giancarlo, *Pro-Reform Reconsideration of the CFTC's Swaps Trading Rules: Return to Dodd-Frank* (Jan. 29, 2015) at p.9.

6 *Id.* at p. 15.

7 *See* Riggs, Onur, Reiffen and Zhu, *supra* note 2, at p. 2 ("We find that the CLOB mechanism has very low trading activity on both SEFs [Bloomberg SEF and Tradeweb SEF] in our sample.").

8 *See* Request for Comment, 83 Fed. Reg. at 61572.

PTNGU Supports Principal Liquidity Provision in Swaps

Anonymous order books with PTNGU attract liquidity by satisfying the needs for principal liquidity providers to have an outlet where they can stream and view available liquidity without attribution while also remaining informed about their counterparties with whom they have executed trades. This method of execution allows dealers to assess over time and across liquidity pools how their liquidity and capital are being allocated amongst their client and dealer relationships and, therefore, to more accurately price the liquidity provided to their clients.

Subjecting all participants and/or liquidity pools to uniform trading requirements (such as banning PTNGU in all instances) therefore may not result in the aggregation of dispersed liquidity or attract new liquidity. In fact, it may result in the reduction of aggregate liquidity and efficiency as participants (*e.g.,* dealers) may be discouraged from trading on anonymous SEFs without PTNGU.

Relatedly, restricting the ability of dealers to determine for themselves how to manage their risk and taking action that might reduce liquidity in pools where they are comfortable trading that risk may reduce the availability of the principal liquidity they provide to the market and thereby increase the likelihood of volatility. While all market participant types and forms of liquidity provision should be encouraged so as to maximize liquidity (buy-side and sell-side, agent liquidity providers and principal liquidity providers), the presence of dealers able to take on risk as principal with strong capital support and willingness to remain engaged in the market during periods of volatility in support of their clients is critical to stemming prolonged market volatility and ensuring systemic stability.

Wider overall spreads or less dependable liquidity on markets that have traditionally served as a risk outlet among dealers is likely to worsen pricing that dealers can offer to clients. As the SEF Proposal recognizes, "dealers base their prices on the cost of hedging those trades in the [D2D] markets."[9] Supporting the removal of PTNGU could result in a severe disruption of both the liquidity-creation process and the allocation of such liquidity to dealer's clients which would certainly have a negative effect on the market.

The Current Market Structure Benefits Market Participants

As noted above, available evidence supports the view that the current market structure, including SEFs that tend to attract distinct D2D and D2C activity, has, overall, benefitted market participants through tighter pricing and increasingly deep liquidity.[10] Nonetheless, some have argued that PTNGU inappropriately encourages bifurcation in the market between D2D and D2C SEFs.

The implication of this argument is that a "bifurcated market" is detrimental—when in fact it is central to supporting less liquid, principal-based markets with diverse products like those under consideration here. Unlike other financial products, swaps are not

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[9] *Id.*

[10] *See* note 2, *supra.*

standardized widgets that dealers must source in bulk so that they can be traded at mark-ups to end clients. Dealers provide liquidity to clients and then hedge residual risks in the D2D market. The relatively worse pricing on D2D SEF order books[11] and lack of trading in fully anonymous order books available on D2C SEFs[12] underscores the point: dealers are incentivized and able to provide their best pricing to clients with whom they have strong relationships, and dealers do not have relationships with anonymous parties on order books.

Indeed, the Commission has recognized the different functions of D2D and D2C SEFs, with certain SEFs favored by "corporate end-users and other buy-side participants [to] manage risk positions that are unique to their particular circumstances [and where] swap dealers provide liquidity to the participants within this segment for a fee […] that reflects the risks incurred by dealers from the episodic or relative lack of liquidity in the swaps market for many specific swaps."[13] On the other hand, other SEFs are primarily used by dealers to "offset positions established through the dealer-to-client market segment by hedging their swaps inventories on a portfolio basis […]."[14]

We also note that the Dodd-Frank Act did not identify nor direct the elimination of the ability for similarly situated market participants from trading with one another. Nor did it direct the elimination of PTNGU, which existed at that time the Dodd-Frank Act was enacted. In addition, the SEF Proposal expressly recognizes the Commission's view supporting the need for platforms addressing the needs of specific market participants to exist, clarifying that it does not view impartial access requirements as a way to promote an "all-to-all" trading environment.

<u>PTNGU Does Not Result In Inappropriate Information Leakage</u>

Some have argued that PTNGU may deter buy-side participation on SEFs where it is utilized due to the prospect of "information leakage", whereby disclosing the identity of a market participant could potentially expose the participant's trading intentions, strategies, positions, or other sensitive information to competitors or dealers. However, information leakage occurs when a participant's activity is revealed without their knowledge or consent. For example, were a participant's trades revealed when executed in an anonymous order book without PTNGU, that would indeed constitute information leakage and present an issue worthy of regulatory action. There are no impediments, nor should there be, to market participants (buy- and sell-side) from trading, should they choose, today in anonymous order books that do not provide PTNGU.

However, participants in anonymous order books with PTNGU understand the rules of those order books up front and, specifically, it is understood that their identity will be revealed to their counterparty. They choose to trade with that knowledge and, in fact, value this feature. Simply because participants in these pools prefer to submit their prices into the order book anonymously, this should not be misinterpreted to imply that their preference or

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11 *See* Collin-Dufrense, Junge and Trolle, *supra* note 2.

12 *See* Riggs, Onur, Reiffen and Zhu, *supra* note 4.

13 SEF Proposal, 83 Fed. Reg. at 61995.

14 *Id.*

intent is to have their identity kept from the counterparty with whom a trade is consummated.

PTNGU Is Not Solely Justified by Credit Risk Considerations

Some have argued that PTNGU was solely motivated by a need for counterparties to know their credit exposure and to book their trades before clearing was required. However, those were not the sole motivations. Knowing one's counterparty to a completed trade was and remains an attractive attribute of order books with PTNGU, for the reasons stated earlier.

Further, even in connection with cleared swaps, there are frequently operational, credit/settlement, and legal considerations that necessitate PTNGU. For example, PTNGU helps enable parties to address operational errors and resulting risks. In addition, certain package transactions involving securities (such as U.S. Treasury swap spreads) or non-cleared swaps typically necessitate PTNGU to address the risks associated with the non-cleared legs of those transactions.[15]

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As the foregoing illustrates, intervening to prohibit PTNGU would raise serious concerns for many market participants, which we urge the Commission to consider as it weighs whether to take further action in this area.

If you have any questions concerning our comments, please feel free to contact the undersigned. SIFMA welcomes the opportunity to discuss these issues further with the Commission and its staff.

Sincerely,

Kyle Brandon
Managing Director, Head of Derivatives Policy
SIFMA

[15] Although fully anonymous trading fully takes places between members of the Fixed Income Clearing Corporation ("**FICC**"), requiring such trading to take place in transactions involving one or both parties who are not FICC members would necessitate intermediation by a clearing broker-dealer and present material systemic risk to that broker-dealer.