ISDA Safe, Efficient Markets

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June 10, 2022

Submitted Electronically

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 20549-1090

Re: *Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities* [Release No. 34-94615; File No. S7-14-22]

Dear Ms. Countryman:

The International Swaps and Derivatives Association, Inc. ("**ISDA**")[1] and Securities Industry and Financial Markets Association ("**SIFMA**")[2] (together, the "**Associations**") appreciate the opportunity to submit these comments on the *Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities* ("**Proposed Rules**") published by the U.S. Securities and Exchange Commission ("**SEC**" or "**Commission**") in the Federal Register on May 11, 2022,[3] pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank Act**" or "**Title VII**").[4]

We applaud the Commission's intent to meaningfully align its approach to the execution of security-based swaps (**"SBS"**) and regulation of security-based swap execution facilities ("**SBSEFs**) with the rules applicable to swaps and swap execution facilities (**"SEFs"**) implemented by the U.S. Commodity Futures Trading Commission (**"CFTC"**).

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[1] Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 980 member institutions from 78 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and depositories, as well as law firms, accounting firms and other service providers. Additional information on ISDA is available at http://www.isda.org.
[2] 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.
[3] 87 Fed. Reg. 28872 (May 11, 2022), *available at* https://www.govinfo.gov/content/pkg/FR-2022-05-11/pdf/2022-07850.pdf [hereinafter, Proposed Rules].
[4] Pub. L. No. 111-203 (2010). Unless the context requires otherwise, general references to Title VII shall refer to Subtitle B, which amends the U.S. securities laws.

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We support the Commission's decision to model the SBS trading framework after the CFTC's SEF regime, which has been up and running for nearly a decade and thus withstood the test of time. Harmonizing with the CFTC's regulatory framework allows market participants to minimize compliance burdens by integrating the SEC rules into their existing compliance frameworks through making adjustments to existing trading procedures and mechanisms, rather than building out separate systems.

Having said so, we also believe that given the size of the SBS market, a more tailored approach may be necessary. We agree with the Commission that SBS markets are significantly smaller and have fewer market participants,[5] as compared to swaps markets.[6] As the Commission notes, just a handful of SEFs intend to register as SBSEFs, since only a minority of SEFs currently offer trading in SBS.[7] In addition, the Proposed Rules would only apply to a handful of US market participants, and certain non-US market participants, which represent only a segment of an already small market, as compared to its swaps counterpart. Moreover, the SEFs that do offer trading in SBS estimate that they have approximately 50 or less trades per day in SBS.

In general, we believe that the final rule will benefit from providing a more nuanced approach to the SBS market, while eliminating any divergences or inconsistences in the areas where there is no need to account for the unique nature of the SBS market. Separately, we note that it is difficult to opine on the substance of the Proposed Rules without knowing what particular types of SBS products would be subject to mandatory trading.[8]

Thus, we have identified some areas of concern and make the following recommendations:

1. <u>Trade Execution Rules</u>: Our comments advocate for a tailored application of certain aspects of the trading rules given the thin nature of SBS markets as compared to swaps markets. We ask that the SEC to:
    a. Allow various stakeholders (and not just SBSEFs) to have input into determining whether a certain SBS product should be subject to the trade execution requirement—the made available to trade (**"MAT"**) process.
    b. Allow a phased-in compliance period for the required methods of execution requirement and temporarily permit a Request-for-Quote-to-One (**"RFQ-to-1"**) system in order to avoid adverse impacts on liquidity.
    c. Revise the proposed block threshold to account for the various liquidity profiles of SBS products.

[5] While there are over 40 registered security-based swap dealers, not all such security-based swap dealers are consistently active in trading SBS. Trading activity in the SBS markets tends to be more concentrated among a subset of such registered security-based swap dealers which increases liquidity concerns in these markets. In contrast, as of March 31, 2022, there are 107 CFTC-registered swap dealers.
[6] Proposed Rules at 28875.
[7] Proposed Rules 28945-46.
[8] Throughout this letter, we provide data-driven evidence and examples that relate to credit SBS; this is because equity derivatives are generally not cleared today, and thus, the immediate impact on those products is less apparent. Should any equity SBS become subject to clearing, we believe that there should be an appropriate period of time for review, including notice and comment, in order to determine how such products would perform under the SEC's trading rules.

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   d. Develop a framework for identifying what types of package transactions should be exempted from mandatory trading and the required methods of execution.
   e. Abandon the proposed Daily Market Report requirement, as its price transparency benefits are minimal as compared to its potential negative impact on the already illiquid SBS market.

2. Cross-Border Rules: We continue to believe that the risk associated with transactions between non-U.S. persons that are arranged, negotiated or executed by U.S. personnel (**"ANE Transactions"**) lies outside the U.S. financial system, and thus, authorities in home jurisdictions of the non-U.S. persons involved have the greater supervisory interest in regulating these transactions. We are also concerned that the Proposed Rules capture other non-U.S. entities and set out overly restrictive conditions for recognizing trading venues. Thus, we ask that the Commission:
   a. Reconsider its approach to: (i) the application of mandatory trading rules to ANE Transactions; and (ii) requiring foreign platforms to register as SBSEFs when executing ANE Transactions;
   b. Reconsider its approach to: (i) the application of mandatory trading rules to Guaranteed Entities[9] and foreign branches of U.S. entities when trading with non-US counterparties; and (ii) requiring foreign platforms to register as SBSEFs when Guaranteed Entities or foreign branches of U.S. persons trade with non-US counterparties.
   c. Exempt foreign trading venues from SBSEF registration requirements where such venues are already exempt from the SEF registration requirements and are in good standing with the CFTC.

3. SBSEF Requirements: While we appreciate the Commission's decision to model the SBSEF rules after the CFTC SEF rules, there are areas where further alignment is necessary to promote SBS trading and reduce unnecessary complexity, costs, and other burdens that impede centralized trading in SBS products. To this end, as described in more detail below, the Commission should:
   a. Abandon the proposed 20% voting cap requirement.
   b. Allow sufficient time for compliance with the SBSEF framework.
   c. Provide further flexibility in the SBSEF registration process.

4. SBSEFs and Securities Exchanges: With respect to the proposed exemption from registration as a national securities exchange, we ask that the Commission eliminate the condition that the entity must be registered as an SBSEF. This would ensure that an organization making available certain methods for parties to interact only in connection with SBS—but no other types of securities—would not become subject to registration as a national securities exchange.

[9] The term "Guaranteed Entity" as used herein is defined as "a non-U.S. person whose performance under an SBS is guaranteed by a U.S. person." Proposed Rules at 29001.

Below, we further explain our recommendations, which will allow the Commission to finalize the Proposed Rules in a way that avoids unnecessary market fragmentation and negative impacts on liquidity in SBS markets, while still meeting the Commission's policy objectives.

I. Trade Execution Rules

A. Enable Member Input in the MAT Process

We have long-held the view that one of the shortcomings of the MAT process is that it puts too much responsibility in the hands of the trading platform, and does not require, or even consider, input from market participants.[10] The implications of this outcome are even more evident in the context of an SBS MAT determination as such determination would only be relevant to a small segment of the global SBS market, and as we noted above, the SBS market is much smaller and less liquid than its swaps counterpart. [11]

Similar to the CFTC's process, the proposed MAT process would require an SBSEF to evaluate an SBS product's performance or activity on its platform (i.e., frequency or size of transactions) which may not necessarily be indicative of an SBS product's trading activity on other platforms, let alone on a global scale. Since market participants trade in SBS markets globally and have experience trading SBS both on and off-platform, they are well-positioned to help determine whether an SBS product is fit for mandatory trading.

For instance, we do not believe that equity SBS products are suitable for mandatory trading due to their bespoke nature. The market value of equity SBS products is derived from their ability to be tailored to fit a variety of client needs, including intra-day liquidity. Once clients choose their dealer counterparties, swap profiles are set and can be utilized daily without additional negotiation. This flexibility is important because it enables counterparties to change details mid-trade based on client needs or changes in market conventions (i.e., moving off of LIBOR and re-rating of swaps). As such, these products are distinct from CFTC equity swaps, which are less customized.[12] Similarly, we do not believe it is appropriate to treat all credit SBS products uniformly. As to CDS products, while there is arguably sufficient standardization in certain CDS products to justify a platform execution framework, the single-bond or single-loan TRS product

[10] We have repeatedly raised this issue and the comments that follow since the MAT process was first established by the CFTC in 2013.

[11] We support the Commission's proposal to require that SBSEFs provide counterparties with a written record of the terms agreed to on the SBSEF, as opposed to the CFTC's attendant requirement that would, from a practical perspective, impose burdensome requirements on SEFs to obtain pre-established agreements between counterparties. As we have argued in the past, the obligation to supplement the terms agreed to on the trading platform should fall on the counterparties themselves, who are familiar with such terms and have them readily available at their disposal. Requiring counterparties to submit previously negotiated terms and/or agreements to an SBSEF is unnecessary and costly. *See* ISDA Response to CFTC Project KISS 82 Fed. Reg. 23765 (Sept. 29, 2017) *available at* https://www.isda.org/a/nVKDE/ISDA-KISS-Response_29-September-2017_Appendix_Links_version_FINAL.pdf.

[12] There have a been a few attempts at creating standardized centrally cleared/listed products meant to replicate SBS equities (i.e., One Chicago single stock Futures – now defunct and Eurex Futures) and they were unsuccessful given that there was no ability to tailor the product to suit clients' need.

tends to be customized on a case-by-case basis. We do not therefore believe mandatory trading is suitable for those products either.

Since SEF trading started almost a decade ago, market participant have consistently requested that the CFTC make adjustments to its MAT process as it has been subject to continuous criticism; and some public sector officials and the CFTC Market Risk Advisory Committee (**"MRAC"**) have called into question its efficacy.[13] Although the CFTC has yet to adopt market participants' recommendations, we ask the Commission to review the CFTC MRAC's recommendations with an eye towards adopting a more flexible regime given the unique characteristics of the SBS market.

Separately, in our experience with the MAT requirement, we have observed that 30 days does not provide sufficient time to adjust trading protocols and ensure a smooth transition to trading on SEFs. In this regard, we ask that the Commission extend the time between when a MAT determination is made and when mandatory trading becomes effective from the proposed 30 days to 90 days. This recommendation is consistent with the recommendations of the CFTC MRAC report that examined the appropriateness, efficacy, and sustainability of the MAT process.[14]

For these reasons, if in the final rule, the MAT requirement remains a precursor to SBS being traded on a SBSEF *via* the required methods of execution, the MAT process should allow market participants—and not just SEFs—to provide input into the SBSEF's decision-making process to ensure that MAT determinations reflect the views of a cross-section of the SBS market. Additionally, we ask the Commission to extend the timeframe in which a MAT determination becomes effective to 90 days.

B. Adopt a Phased-In Approach to the Required Methods of Execution

While market participants have traded under the current trade execution regime for almost ten years, we believe that in the case of SBS products, the Commission should take a more nuanced approach to SBSEF trading and not immediately impose the required methods of execution. As proven by experience, the MAT self-certification process does not provide a sufficient check on

[13] *See* Recommendations Regarding the "Made Available To Trade" (MAT) Process, Report of the Market Structure Subcommittee, Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission (February 2021), *available at* https://www.cftc.gov/media/6191/MRAC_MSSRRMP022321/download; *see also* U.S. Department of the Treasury, A Financial System That Creates Economic Opportunities: Capital Markets at 145 (Oct. 2017), available at https://www.treasury.gov/press-center/press-releases/documents/afinancial-system-capital-markets-final-final.pdf (Treasury acknowledged market participant's concerns that that the six factors that SEFs must consider before making a MAT determination are not robust enough to demonstrate sufficient liquidity for mandatory trading, and therefore recommended that the CFTC "reevaluate the MAT determination process to ensure sufficient liquidity for swaps to support a mandatory trading requirement.").

[14] *See* Recommendations Regarding the "Made Available To Trade" (MAT) Process, Report of the Market Structure Subcommittee, Market Risk Advisory Committee of the U.S. Commodity Futures Trading Commission (February 2021), *available at* https://www.cftc.gov/media/6191/MRAC_MSSRRMP022321/download.

listing new products and could easily list products that do not have the liquidity to be traded *via* more restrictive methods of execution.

When considering the lack of liquidity in SBS products, pre-trade price transparency *via* the proposed request-for-quote-to-three (**"RFQ-to-3"**) requirement could negatively impact liquidity provision for end-users. We are concerned that if clients are required to show their hand to three liquidity providers, it may lead to information leakage and an inability to hedge their risks through SBS markets. This is particularly so given that for many SBS products there are only a relatively small number of active dealers. For example, based on DTCC data on credit SBS, for the top 700 issuers there are on average 2.7 dealers and 400 of the top 700 issuers have fewer than three active dealers per month.[15] If executing mandatory traded SBS contracts is not an economically viable option for market participants, given current SBS trading volumes and liquidity, market participants may simply choose to exit the market.

An RFQ-to-3 requirement would also be problematic for SBS equities, where current execution processes are very different from their swaps counterpart. A client will simply ask its preferred dealer to execute an "X" share SBS at market price (or some other pricing structure). Dealers will then purchase the shares directly for hedging purposes and execute the swap at the end of the day with the client at an average market price (assuming the client submitted multiple requests over a single day, which is common market practice). At the onset of the relationship, clients will negotiate a grid with dealers where certain short/long benchmarks and spreads are agreed for equity issuers on a jurisdictional or other basis. In this case, the dealer's interaction is more akin to a broker than a dealer counterparty. These trading practices and counterparty exchanges, would not be possible on an RFQ-to-3 or order book system.

Additionally, we compared the credit swaps activity that occurred on-venue back in 2012 before the CFTC trade execution requirement kicked in, with the credit SBS activity that occurs on-venue today. The result is that 48.2% of AMRS CDX trading client volume was on-venue in 2012; while YTD 2022 shows that only 4.9% of AMRS SNCDS trading client volume occurred on-venue.[16] This shows that the swaps market was much more ready for the implementation of the trade execution requirement than the credit SBS market is today. Absent a phased-in implementation approach, the SBS market could suffer from significant disruptions.

For these reasons, the Commission should provide "phased-in compliance" with the required methods of execution, whereby a MAT SBS product may be executed on an SBSEF *via* any method of execution until such time when it is determined through notice and comment that an appropriate level of liquidity exists to enable an order book or RFQ-to-3 system.

[15] https://www.dtcc.com/repository-otc-data/top-1000-single-names-12-20-2021-through-03-19-2022.
[16] One ISDA member provided this analysis based on their clients' index-based CDS and SNCDS executions over the stated time periods. ISDA members agree that this data is representative across all market makers.

C. Re-evaluate the Proposed $5 Million Block Threshold

We support the Commission's proposal to provide an exemption for block trades and the alignment of the block trade definition with the CFTC's definition. As the Commission correctly points out, the purpose of providing an exemption for block trades from mandatory trading protocols is to balance the promotion of price competition with the preservation of market liquidity.[17]

The Proposed Rules impose a $5 million block trade threshold for SBS based on a single credit instrument or a narrow-based index of credit instruments,[18] but provide no explanation as to how the Commission arrived at this number —other than noting that the threshold was established based on the $5 million cap that Financial Industry Regulatory Authority applies to cash debt securities.[19]

As a general matter, before proposing block thresholds, the Commission should first establish an appropriate methodology to determine block thresholds based on current market-wide data. Otherwise, the already illiquid SBS market will be required to comply with an arbitrary, "one-size-fits-all" threshold amount that fails to consider the unique levels of market liquidity and risk sensitivity of various instruments.

In order to support our assertion that the Commission's proposed block threshold for credit SBS should be recalibrated, we conducted an analysis of CDS data derived from DTCC Trade Information Warehouse from September 2021 to December 2021. The analysis compares average daily volume (**"ADV"**) in single-name CDS and broad-based index CDS.[20] We believe that ADV is an appropriate indicator of liquidity levels because it represents a measure of how much trading occurs in a given issuer across the market as a whole. In other words, the lower the ADV, the lower the liquidity of the product.

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[17] Proposed Rules at 28895.
[18] Proposed Rule 802.
[19] Proposed Rules at 28896.
[20] DTCC Trade Information Warehouse (TIW) data provides weekly global transaction activity for index CDS and single-name CDS. The transactions covered in this analysis include only transactions where market participants were engaging in market risk transfer activity. Risk transfer activity is defined as transactions that change the risk position between two parties. These transaction types include new trades between two parties, a termination of an existing transaction, or the assignment of an existing transaction to a third party. DTCC TIW Weekly Transaction Activity report captures only weekly market activity for single-names and indices with 10 contracts or greater in the warehouse. The analysis covers the period from September 20, 2021, to December 31, 2021. The analysis specifically looks at CDX.NA.IG.37, CDX.NA.HY.37, and ITRAXX EUROPE S36, which were at the time the on-the-run credit indices. Total traded notional is calculated as the sum of weekly transaction activity for index CDS and single-name CDS, respectively. Total trade count is calculated as the sum of number of contracts. ADV is calculated by dividing total traded notional by 70. For single-name CDS, ADV is calculated at an issuer-level. Average daily trade count is calculated by dividing total trade count by 70. Average trade size is calculated by dividing total traded notional by total trade count. The analysis was performed by the ISDA Research team. For more details, please see the Appendix.

The analysis showed that the ADV, and therefore liquidity, in single-name CDS is significantly lower than broad-based index CDS.[21] It also showed that liquidity in single-name CDS was concentrated in the most actively traded sovereign issuers. Specifically:

- ADV for NA IG single-name CDS per issuer is about 3200x smaller than for CDX.NA.IG index
- ADV for NA NY single-name CDS per issuer is about 1400x smaller than for CDX.NA. HY index
- ADV for European IG single-name CDS per issuer is about 2400x smaller than for ITRAXX EUROPE index
- ADV for corporate single-name CDS issuers was about 8x lower compared to sovereign issuers

This means that it would take longer for a liquidity provider to offset positions in single-name CDS than in an index CDS. Thus, we do not think it is appropriate for the Commission to mirror its block threshold for credit SBS to a cap threshold that was established for debt securities—an entirely separate market—when there are clear differences in liquidity levels within the CDS market itself.

Also, the data revealed that liquidity in single-name CDS is disproportionately concentrated in the most actively traded issuers. Specifically:

- ADV for the 10 most actively traded NA IG single-name CDS issuers included in CDX.NA.IG index is 3x greater than for the rest of index constituents
- ADV for the 10 most actively traded NA HY single-name CDS issuers included in CDX.NA.HY is 3.5x greater than for the rest of index constituents
- ADV for the 10 most actively traded European IG single-name CDS issuers included in ITRAXX EUROPE is 3.6x greater than for the rest of index constituents

This corroborates our assertion that block thresholds should be calibrated at a more granular level in order to reflect the different liquidity levels of credit SBS products.

Absent a data-based approach to setting block thresholds for SBS credit instruments, the proposal runs the risk that $5 million may be an inappropriately high threshold for credit SBS, which may widen bid/offer spreads, further reduce liquidity, and will force large-sized transactions to be publicly reported with their full size. As the Commission acknowledges,[22] forcing a dealer that has transacted in a larger order to expose its position to SBSEF participants (*via* RFQ-to-3 or order book) runs the likely risk that the market will move against that dealer before the dealer is able to adequately lay-off its exposure (commonly referred to as the "winner's curse").

[21] For more details, please see the Appendix.
[22] Proposed Rules at 28895-96.

Liquidity providers will need to account for the "winner's curse," and as a result, the cost of transacting with immediacy will rise substantially, leading to overall increased costs and time delays in executing hedges, and adding to or taking down positions. Higher prices or reduced liquidity (or both) will have a direct impact on clients and end-users who will ultimately bear the increased costs and inefficiencies incurred when forced to split large trades into smaller sizes for liquidity purposes. More likely, these clients, end-users and/or liquidity providers may decide that it is more economical to exit the market entirely given that most of them do not trade in large volumes of SBS.

Separately, we note that if an equity SBS product becomes subject to mandatory trade execution, we believe that establishing an appropriate methodology for establishing equity block thresholds would be necessary to avoid the same outcomes discussed in this section.

Accordingly, the Commission should reevaluate its block thresholds for SBS credit instruments and develop a methodology for determining appropriate block thresholds that takes into account the relationship between volume, frequency, liquidity and risk sensitivity of each instrument, rather than imposing a blanket, arbitrary threshold.[23]

D. Create a Formal Process for Package Trade Exemptions

The Proposed Rules would codify an approach to package transactions drawn directly from the CFTC's rules to such transactions. Although we agree that it is appropriate to treat package transactions differently from outright, or single-legged, transactions, it is unlikely that the CFTC's specific rules for identifying particular types of package transactions and tailoring execution protocols for such transactions would be appropriate for SBS. Those rules were developed by the CFTC, initially *via* staff no-action relief, after SEFs had adopted various MAT determinations and market participants had provided input to the CFTC regarding the particular types of package transactions common in the marketplace for the relevant types of MAT swaps. It is for this reason that the particular types of package transactions addressed by the CFTC generally focus on transactions common in the interest rate swap market, which comprise the majority of MAT swaps. In addition, the current state of the CFTC's rules in this area reflects the culmination of a phased implementation approach developed over time *via* no-action letters.

In light of this, it would be better for the Commission to tailor its rules for package transactions to address the particular market dynamics relevant to the SBS market instead of those in the swaps market. We recommend that the Commission build into the MAT determination process a

[23] As the appropriate block threshold depends on factors such as liquidity and risk sensitivity which can change over time, we believe that the rules should provide a formal adjustment mechanism that would allow market participants to petition the Commission to temporarily change block thresholds based on observed market conditions, or enable the Commission's staff to do so, subject to a public comment process. Notably, in the swaps market, the COVID-19 crisis reinforced the need for regulators to be able to quickly exercise flexibility and adjust block thresholds during a time of diminished trading liquidity. During the crisis, our members observed that it had become increasingly difficult to execute large-sized transactions on a SEF *via* an RFQ-to-3 due to the limited availability of market makers and diminished trading liquidity. The result was that firms were forced to break up large SEF-mandated trades into smaller, more liquid trades—resulting in increased costs and inefficiencies.

framework for identifying what types of package transactions exist for prospectively MAT SBS and then develop tailored rules around the execution of such transactions.

E. Abandon the Proposed "Daily Market Report"

The Proposed Rules require SBSEFs to publish a "Daily Market Report" that includes both specific and aggregated information related to volume, pricing, and block trades. As a preliminary matter, we see no reason why such a report is necessary. We believe that the SEF regulatory framework, which does not impose such a requirement, provides sufficient price transparency. The Commission has not pointed to any observable issues with the SEF transparency framework to justify a need for these reports.

Specifically, we are concerned that the daily publication of information related to block trade numbers and block notional amounts, coupled with aggregate pricing information, would magnify the problems associated with the "winner's curse" (as described above).

This is particularly concerning where a dealer is unable to fully lay-off its risk from a block trade within the course of a single day—a scenario that is extremely likely considering the thin nature of SBS markets. Based on the information published in the report as proposed, SBSEF participants may be able to identify a particular block trade and the likely price point, and then use such information to up-charge the dealer who is seeking to lay off the rest of its risk, thus frustrating the key objective of block trading.

These issues are amplified even further if the Daily Market Report does not follow the cap requirements that apply in the public price dissemination of data under the Commission's trade reporting rule and related SEC no-action relief. Publication of uncapped trade sizes could, in certain cases, reveal the exact notional amount of a trade to the public, which is not permitted under the Commission's SBS trade reporting rules.[24] For example, in the simplest case, if only one block trade (that also reaches or surpasses the cap size) for a certain class of SBS is traded on a given day, the proposed Daily Market Report would reveal the exact notional amount of such trade. This is especially concerning given that the proposed Daily Market Report provides detailed information by SBS product and tenor.

Thus, we ask the Commission to abandon its proposed Daily Market Report in the final rule. If the Commission decides to move forward with this part of the Proposed Rules, we would strongly recommend that the proposed report be published on a monthly or quarterly basis, instead of daily. In any case, we ask that the Commission explicitly clarify that the Daily Market Report is subject to the cap size requirements imposed on SBSDRs. This would ensure that the report does not conflict with the protections afforded to market participants per the cap size requirements and under the Commission's SBS trade reporting rules and related relief for SBS.

[24] Under the Commission's trade reporting rule and related relief, if an SBS reaches the cap size, the true notional of the SBS will not be made available to the public at any time, but only the cap size would be revealed.

II. Cross-Border Application of Trading Rules and SBSEF Registration Requirements

A. ANE Transactions Should Not Be Subject to Mandatory Trading or Trigger SBSEF Registration

We continue to strongly believe that transactions between two non-U.S. persons where one person uses U.S. personnel to arrange, negotiate, or execute the transaction (**"ANE Transactions"**), and where no further U.S. nexus exists, fall outside the jurisdictional reach of Title VII. However, in the Proposed Rules, the Commission reiterates its view that it has jurisdiction over ANE Transactions. Specifically, with respect to SBS trading rules, the Commission: (1) applies its trade execution mandate to ANE Transactions;[25] and (2) requires that foreign trading venues register (or get an exemption from registration) as an SBSEF if they offer services to "covered persons"[26] which include participants that engage in ANE Transactions.

We continue to insist that the location of personnel or agents within the United States should not form the basis for extending the SEC's trading mandate or requiring SBSEF registration. When assessing whether it is necessary to extend the extraterritorial reach of a particular ruleset, it is important to consider the objectives of individual rulesets. In the context of centralized swap trading, as we noted above, platform trading rules are not intended to address or mitigate risk, and therefore, the Commission should exercise more flexibility when deciding whether the SEC trading rules should extend to ANE Transactions that already have an attenuated connection to the U.S. For the same reasons, ANE Transactions executed on a foreign trading platform should not trigger SBSEF registration requirements.

As we have submitted in the past, rules related to mandatory platform execution are intended to provide counterparties with a sufficient level of pre-trade price transparency, and rules related to platform registration are intended to improve market structure. While these are important policy goals, they should be addressed by the market regulators in the jurisdiction where the majority of the trading activity is taking place.

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[25] The proposed application of mandatory trading requirements to ANE transactions is especially troubling considering that the Commission considered this issue extensively several years ago, ultimately deciding in 2015 to withdraw an earlier 2013 proposal to subject ANE transactions to those requirements. The Commission made this decision because "the financial risks of such a transaction reside outside the United States" between non-U.S. persons and therefore the Commission did "not believe it appropriate to require such non-U.S. persons to shift their non-U.S. business to trading platforms merely because one of the counterparties to the transaction sues personnel located in a U.S. branch or office to arrange, negotiate, or execute the transaction." That rationale applies equally today.

[26] We appreciate that the Commission has clarified that the "covered person" definition is a transaction-based test. However, we believe that the proposed rule text could be more explicit in this regard. Thus, we propose that the Commission adopt the definition as follows: "a 'covered person' means, with respect to a particular security-based swap, any person that is: (1) A U.S. person; (2) A non-U.S. person whose performance under ***that*** security-based swap is guaranteed by a U.S. person; or (3) A non-U.S. person who, in connection with its security-based swap dealing activity, uses U.S. personnel located in a U.S. branch or office, or personnel of an agent of such non-U.S. person located in a U.S. branch or office, to arrange, negotiate, or execute ***that security-based swap transaction***."

Applying these requirements to ANE Transactions, a term the Commission has broadly interpreted, would bring a random selection of additional transactions into scope merely due to some supporting role played by a U.S. based sales person, trader or other function caught up in ANE. Neither the platform nor the counterparty would be aware of ANE in most instances. Given the risks of running afoul of these requirements, in practice, firms and platforms would be required to make representations that no ANE touchpoint is present in the U.S. for any SBS subject to the trading mandate. This, in turn, would require the development of a costly parallel infrastructure completely devoid of U.S. touchpoints for what will remain for the foreseeable future a small sliver of the overall SBS market.

In addition, since the 2008 financial crisis, jurisdictions across the globe have adopted robust regulatory regimes that apply to *both* non-US persons and foreign trading venues. And yet, the Proposed Rules do not recognize that these transactions and entities are already subject to comparable and comprehensive regulations in their respective jurisdictions.[27] The Commission's far-reaching proposal to subject ANE Transactions to mandatory trade execution and apply SBSEF registration requirements to foreign platforms that execute ANE Transactions would result in market participants facing dual and competing obligations that are not supported by any policy or risk mitigation objectives. Moreover, the Proposed Rules stand in stark contrast to recent efforts by the CFTC to curtail the U.S.' approach to extra-territoriality in light of the progress made by other jurisdictions in establishing robust derivatives regulatory regimes.[28]

For these reasons, we urge the Commission to reconsider its proposal to apply mandatory trading to ANE Transactions, and use ANE Transactions as a trigger for foreign venue registration.[29]

B. Guaranteed Entities and Foreign Branches of U.S. Persons Should Not Be Subject to U.S. Mandatory Trading Rules or Trigger the Registration of Foreign Trading Venues

The Proposed Rules extend the trade execution requirement to non-U.S. persons that are guaranteed by U.S. person (**"Guaranteed Entities"**) and foreign branches of U.S. persons, when trading with non-U.S. persons, reasoning that SBS trading activity conducted by these entities pose risk to the U.S. financial system.[30] We disagree. To reiterate, mandatory trade execution is not designed to address or mitigate systemic risk. Thus, it is not necessary to extend SBSEF rules across the globe, to overseas transactions with non-U.S. counterparties, where the lack of such rules would have no ability of posing risk to the U.S. financial system.

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[27] *See* ISDA Cross-Border Harmonization Paper (listing key derivatives requirements from a broad range of jurisdictions).

[28] In 2020, the CFTC announced its policy that the use of personnel or agents located in the United States to arrange, negotiate, or execute swap transactions with non-U.S. counterparties "would not be considered a relevant factor" for purposes of applying certain rules to non-U.S. dealers, including mandatory trade execution requirements.

[29] At a minimum, the Commission should limit the coverage of these requirements to only include the ANE activity of SBSDs (or entities relying on Rule 3a71-3(d)).

[30] Proposed Rules at 28922-26.

Critically, the Commission's proposed cross-border application of the SBSEF registration requirement would, without justification, depart from the approach the Commission initially proposed in 2013, which itself was drawn from the longstanding Commission guidance regarding when foreign securities exchanges must register with the SEC.[31]

Guaranteed Entities are, by definition, non-U.S. persons and are therefore subject to foreign laws and regulatory authority of their home countries. Similarly, foreign branches of U.S. persons, when trading with non-U.S. persons, are subject to the laws of the foreign jurisdictions in which they and their counterparties operate. Imposing U.S. mandatory trading obligations on these entities (when they are dealing with non-U.S. counterparties) and SBSEF registration requirements on foreign trading platforms that allow these entities to access to their venues will result in the application of duplicative regulation—increasing compliance costs and adding complexity and inefficiencies to cross-border trading.

Further, foreign trading venues are already subject to a comprehensive regulatory oversight in their home jurisdictions. Based on our experience with the CFTC's SEF trading rules, foreign platforms will deny access to any entity with any connection to the United Sates, no matter how remote, for fear of being captured by the SEC's regime. These negative market impacts are too high of a price to pay for a market of this limited size. The likely result will be that foreign trading venues will deny access to Guaranteed Entities and foreign branches. This will lead to further fragmentation of SBS markets. Notably, the CFTC resolved this issue when it granted equivalency to major foreign trading platforms in Europe and Asia.

Accordingly, we believe that Guaranteed Entities and foreign branches of U.S. persons should not be subject to the SEC mandatory trade execution requirements. We also believe that foreign trading venues should not be required to register as SBSEFs if they offer services to Guaranteed Entities or foreign branches of U.S. entities when trading with non-U.S. persons.

C. The SEC Should Automatically Extend SBSEF Registration Exemptions to Foreign Trading Venues Recognized by the CFTC

Over the past few years, the CFTC has achieved significant progress on the cross-border trading front, particularly when it took action to implement mutual recognition of derivatives trading venues. These steps are essential to ensuring strong and stable global swaps markets. The regime of mutual recognition enables U.S. persons to execute their swaps subject to the trade execution

[31] *See Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants*; SEC Release No. 34-69490 (May 1, 2013), 78 FR 30697, 31054-55 (May 23, 2013) (proposing to require a foreign SBS market to register as an SBSEF when it provides U.S. persons, or non-U.S. persons located in the U.S., with the *direct* ability to trade or execute SBS on the foreign SBS market or grants such persons membership or participation in the foreign SBS market).

mandate on foreign trading venues in the EU, UK, Singapore, and Japan pursuant to the local trading rules and protocols of those jurisdictions.[32]

As a result, market participants across these key derivatives trading hubs have enjoyed unfettered access to liquidity in those markets. Today, the decision where to trade the most standardized and liquid swaps is dictated by the available liquidity and prices in global markets. If finalized as proposed, the Commission's approach will have the opposite effect. It will force market participants to trade SBS within the jurisdictional borders of the United States, restricting access to global liquidity and thus further diminishing already thin SBS markets.

The Proposed Rules run counter to the progress made by global regulators over the past decade. They impose an unachievable standard for granting exemptions to foreign trading venues. Specifically, we find the Commission's statement that it would not recognize a foreign trading venue as an Exempt SBESEF if the foreign jurisdiction's rules do not require SBS products that are subject to mandatory platform execution to be executed through means comparable to a central-limit-order-book or an RFQ-to-3 system especially problematic.[33] This approach will likely disqualify the majority of foreign trading venues recognized by the CFTC (**"Exempt SEFs"**). In other words, hardly any (if any at all) foreign trading venues would be able to enjoy an Exempt SBSEF status. To our knowledge, none of the CFTC recognized MTFs or OTFs are required to offer a CLOB on their platforms. In addition, although MIFID II requires MTFs and OTFs to have a least three materially active members or users, each having the opportunity to interact with all others with respect to price formation, there is no mandatory requirement to send a price quote to at least three dealers.

The Commission's reasoning for not immediately extending its exemptive authority to the 53 Exempt SEFs is that the statutory language of its exemptive authority differs from the CFTC's authority. The SEC is statutorily required to grant exemptions that are "necessary or appropriate in the public interest, and consistent with the protection of investors," while the CFTC must find that a foreign trading venue "is subject to comparable, comprehensive supervision."[34]

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[32] CFTC Order of Exemption with respect to Multilateral Trading Facilities ("**MTFs**") and Organised Trading Facilities ("**OTFs**") authorized in the European Union ("**EU**") *available at* https://www.cftc.gov/International/ForeignMarketsandProducts/ExemptSEFs; CFTC Order of Exemption with respect to approved exchanges ("AEs") and recognised market operators ("RMOs") authorized in Singapore, *available at* https://www.cftc.gov/International/ForeignMarketsandProducts/ExemptSEFs; CFTC Order of Exemption with respect to electronic trading platforms ("ETPs") registered in Japan, *available at* https://www.cftc.gov/International/ForeignMarketsandProducts/ExemptSEFs; *see also* CFTC No-Action Letter No. 21-24 (Nov. 17, 2021), *available at* https://www.cftc.gov/LawRegulation/CFTCStaffLetters/index.htm.

[33] Proposal at 28925 (stating that, in the context of granting exemptions for foreign trading venues, "the Commission preliminarily believes that a trade execution requirement in a foreign jurisdiction would not be comparable to the trade execution requirement under the SEA if the foreign jurisdiction's rules dud not require SBS products subject to that requirement to be executed through means comparable to [the required methods of execution] as described in proposed Rule 815 (*e.g.*, if the foreign jurisdiction allowed the use of single-dealer platforms to discharge any mandatory trading execution requirement in that jurisdiction)").

[34] Proposed Rules at 28924.

In our view, the aforementioned technical difference in exemptive authority does not preclude the Commission from automatically recognizing Exempt SEFs as "Exempt SBSEFs." To the contrary, the automatic recognition of Exempt SEFs as Exempt SBSEFs is in the public interest and consistent with investor protection. Failing to extend recognition to Exempt SEFs for SBS products will disrupt current SBS trading on Exempt SEFs. Currently, SBS products are traded on foreign venues recognized by the CFTC, as there are no distinctions in the regulation of swaps and SBS outside of the U.S. Disruption in SBS trading will force market participants out of already significantly illiquid market, further deepening market fragmentation. These market disruption events can hardly be supported by any public policy reason; and the Commission does not provide any justification in the Proposed Rules. As currently drafted, the Proposed Rules run counter to the public interest as the limited liquidity in the SBS market is not going to withstand significant disruptions, increased costs, and market fragmentation, thus making it more likely for market participants to exit the SBS markets entirely.

Moreover, we find the Commission's position on foreign venue recognition somewhat puzzling. On one hand, the Commission intends to implement its SBS trading rules consistent with the existing CFTC's regulatory regime for swap execution in order to "obtain comparable regulatory benefits as the CFTC while minimizing costs imposed on SEF/SBSEFs and their members to the greatest extent practicable."[35] On the other hand, the Commission proposes standards for foreign venue recognition that would make it virtually impossible for SBS products to trade on foreign venues—while a significantly larger segment of the swaps marker has benefited from the equivalence regime, without having any regulatory issues or concerns.

Thus, while the CFTC took a giant leap forward, the Proposed Rules, if finalized, will set us back years in both the public and private sectors' global efforts to harmonize cross-border trading of swaps.

For these reasons, we remain concerned that if the Proposed Rules were to be finalized as is, the Commission would frustrate the progress made over the past years to promote and create efficiencies in cross-border trading. We therefore urge the Commission to recognize Exempt SEFs as Exempt SBSEFs in the final rule. At a minimum, we ask that the Commission adopt a more flexible approach to the recognition of foreign trading venues—one that relies on holistic outcomes and governing principles, rather than a rule-by-rule analysis. In the alternative, in order to avoid duplicative or conflicting regulation, we ask that the Commission grant an exemption from the trade execution requirement if the SBS transaction at issue is subject to mandatory trading in another jurisdiction.

[35] Proposed Rules at 28892.

III. SBSEF Requirements

As noted above, we appreciate that the Proposed Rules acknowledge that closely aligning its registration rules with the CFTC's requirements will enable entities that seek dual registration to only make "minor adjustments to their rules and trading procedures to support trading of SBS in addition to the trading of swaps."[36] However, we are concerned that the proposed 20% voting cap requirement could potentially thwart the Commission's objective to ensure that only incremental changes would be necessary to adopt the SBSEF framework.[37] The proposed cap may require SEFs to set up an entirely new legal entity with a different governance structure, making it more challenging to obtain dual-registration.

We understand that conflicts of interest rules are important to ensure fair and orderly trading markets. However, the conflicts of interest rules implemented by the CFTC, which do not include a 20% voting cap, sufficiently address any conflicts of interest concerns. SEFs have operated under those rules for almost 10 years, and there have been no observable issues that would warrant such a regulatory shift. Imposing these additional requirements would frustrate the Commission's overall policy objective to provide a smooth transition for SEFs to become SBSEFs.

Aside from the proposed 20% voting cap, we agree with the Commission that the SBSEF registration should be a relatively smooth process given the proposed alignment of SEF and SBSEF registration requirements. However, from a practical implementation perspective, SEFs that intend to become dually registered will still need time to make technological and operational adjustments in order to integrate the SEC's framework into its existing systems.

While SEFs will be able to leverage their experiences in implementing the CFTC rules, in practice, any transition to a new (even though familiar) framework is never as straightforward as it appears. For example, SEFs will need to make technological adjustments to their platforms to create order book or RFQ functions to support SBS trading, and then may need additional time to test their systems and provide and test connectivity to their clients' systems. In addition, SBSEFs will need to obtain from their clients the necessary disclosures and representations relating to trading SBS products under the Securities Exchange Act of 1934 (**"Exchange Act"**). Given these logistical complications, we ask that the Commission provide a compliance period of at least one year after the rule is finalized.

In addition, we believe that the final rule would benefit from an even more streamlined registration procedures that would allow SEFs to use their existing CFTC documentation when applying for SBSEF registration. For example, we do not see a need for SEFs that are in good standing with the CFTC to file an entirely separate registration form. Instead, SEFs should be permitted to submit their existing registration SEF Form to the SEC with an addendum reflecting

[36] Proposed Rules at 28882.
[37] Proposed Rules at 28875 (acknowledging that "dually registered entities could utilize their existing systems, policies, and procedures to comply with the Commission's SBSEF rules, and SEF market participants would face no or only incremental changes to trade SBS as well as swaps on those facilities, and to comply with the Commission's rules regarding SBS trading").

changes germane to SBS products and SBSEF registration. We also ask the Commission to allow SEFs that are in good standing with the CFTC to qualify for "temporary registration status" while they are in the process of complying with the SBSEF framework.

Collectively, these adjustments would significantly streamline the transition from SEF to SBSEF, reducing the cost of compliance, and consequently, may encourage more SEFs to become SBSEFs. Accordingly, we ask that the Commission: (i) abandon the proposed 20% voting cap requirement; (ii) afford sufficient time for compliance with the SBSEF framework; and (iii) provide more flexible mechanisms for SBSEF registration.

IV. SBSEFs and Securities Exchanges

The Proposed Rules would amend Rule 3a1-1 under the Exchange Act to exempt an entity from the definition of "exchange" that has registered as an SBSEF and provides a market place for no securities other than SBS, thus exempting such an entity from registration as a national securities exchange. We support this exemption, which is necessary because, as the Commission notes, an entity that meets the SBSEF definition also would likely meet the definition of "exchange" set forth in Section 3(a)(1) of the Exchange Act and the interpretation of that definition set forth in Rule 3b-16 thereunder. Without this exemption, the Exchange Act's regulatory framework for national securities exchanges would subsume and override Congress's carefully tailored regime for regulating execution facilities in the SBS market.

Separately, however, the Commission has proposed to expand Rule 3b-16 substantially so as to define a wide variety of other organizations active in the government securities, equities, and other securities markets as "exchanges." If adopted, that proposal would reverse the previous relationship between "exchange" definition (as interpreted in Rule 3b-16) and the SBSEF definition. As a result, an organization making available certain methods for parties to interact in connection with SBS—but no other types of securities—could become subject to registration as a national securities exchange. Such an organization would not benefit from the SBSEF exemption from the "exchange" definition because it did not meet the SBSEF definition. This anomalous result would, in our view, upset the carefully tailored SBS regime noted above. It would institute a two-tiered framework subjecting certain communications protocols for SBS to a securities exchange regulatory regime designed for other types of securities, whereas other communications protocols for SBS would be regulated as SBSEFs.

Accordingly, we request that the Commission expand its proposed amendments to Rule 3a1-1 to exempt any organization, association, or group of persons providing a market place for no securities other than SBS from the definition of "exchange," regardless of whether such organization, association or group is registered as an SBSEF. This approach would preserve Congressional intent and ensure that only the appropriate entities are subject to the SBSEF registration framework.

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We support the Commission's efforts to harmonize its SBSEF trading rules with those rules applicable to swaps markets. We are strongly committed to maintaining the safety and efficiency of global derivatives markets and hopes that the Commission will consider our recommendations, as they reflect the extensive knowledge and experience of trading professionals within our membership. We recognize that fully implementing the SBS trading regime will require a coordinated effort on behalf of both the Commission and market participants. Both ISDA and SIFMA stand ready to assist the Commission in this important effort.

Please do not hesitate to contact us or Nicolette Cone, Associate General Counsel, ISDA (202-569-5782) should you have any questions or seek any further clarifications.

Sincerely,

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APPENDIX

Table 1: Index CDS and Single-name CDS Transaction Activity

Product	Total Traded Notional (US$ billions)	Total Transaction Count	ADV (US$ billions)	Average Daily Trade Count	Average Trade Size (US$ billions)
Index CDS					
CDX.NA.IG.37	2,650.0	34,547	37.857	494	0.077
CDX.NA.HY.37	705.5	30,206	10.079	432	0.023
ITRAXX EUROPE S36	2,552.7	30,214	36.467	432	0.084
Singe-name CDS					
CDX.NA.IG.37 Constituents (average per issuer)	0.8	185	0.012	3	0.004
CDX.NA.IG.37 Constituents (Total)	102.7	23,186	1.467	331	0.004
CDX.NA.HY.37 Constituents (average per issuer)	0.5	186	0.007	3	0.003
CDX.NA.HY.37 Constituents (Total)	50.6	18,231	0.723	260	0.003
ITRAXX EUROPE S36 Constituents (average per issuer)	1.1	174	0.015	2	0.006
ITRAXX EUROPE S36 Constituents (Total)	132.6	21,805	1.894	312	0.006
All corporate single-name CDS (average per issuer)	0.6	128	0.008	2	0.005
All corporate single-name CDS (Total)	375.2	83,249	5.360	1,189	0.005
All sovereign single-name CDS (average per issuer)	4.5	529	0.065	8	0.009
All sovereign single-name CDS (Total)	221.8	25,905	3.169	370	0.009
All single-name CDS (average per issuer)	0.8	153	0.012	2	0.005
All single-name CDS (Total)	600.6	109,953	8.581	1,571	0.005

Table 2: Indices vs. Single-name CDS Index Constituents

	ADV (x)	Average Daily Trade Count (x)	Average Trade Size (x)
CDX.NA.IG.37 vs. Constituents (average per issuer)	3,226	186	17
CDX.NA.HY.37 vs. Constituents (average per issuer)	1,367	162	8
ITRAXX EUROPE S36 vs. Constituents (average per issuer)	2,406	173	14

Table 3: ADV for Top 10 Single-name CDS Index Constituents vs. the Rest of Index

	Top 10 Issuers ADV (US$ billions)	The rest of Index Constituents ADV (US$ billions)	Difference (x)
CDX.NA.IG.37 Constituents (average per issuer)	0.031	0.010	3.1
CDX.NA.HY.37 Constituents (average per issuer)	0.020	0.006	3.5
ITRAXX EUROPE S36 Constituents (average per issuer)	0.045	0.013	3.6