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Submitted via SEC Internet Comment Form

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Ms. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Joint Request for Comment on Further Definition of "Swap" and "Security-Based Swap" and on Alternative Compliance, File No. S7-2026-21 (RIN 3038-AF71; RIN 3235-AN79)

Dear Mr. Kirkpatrick and Ms. Countryman:

I. Introduction

Thesis Market, Inc. ("Thesis") submits this comment with respect to the above-referenced request for comment ("Joint RFC") of the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") (together, the "Commissions"). Thesis is interested in the trading of event-related products across a range of underlyings, including events and performance metrics related to an issuer. Thesis commends the Commissions for working together to facilitate bringing novel products to market. As both agencies know, in the past, novel products have often languished when they raised jurisdictional questions between the Commodity Exchange Act ("CEA") and the Securities Exchange Act ("SEA"). Legal uncertainty often delays the growth of markets that would otherwise be useful to investors.

II. Summary of Position

Thesis supports the Commissions' efforts to promote greater legal certainty around issuer-related event contract products ("IRECP" or "IRECPs") and the Commissions' harmonization efforts, generally. Thesis particularly appreciates the CFTC's efforts to support oversight and innovation in event markets, which have significantly facilitated their growth. Thesis believes the Joint RFC provides an opportunity to help clarify the regulatory treatment of IRECPs and thereby further support the development of these markets.

Thesis considers an IRECP to be an issuer-related contract that is based on the occurrence, non-occurrence, or extent of the occurrence of an event or the measurement of a performance metric related to a specified issuer's business. A central challenge facing IRECP markets is uncertainty regarding where particular products fall across the jurisdictional lines of the CFTC and SEC. In terms of the existing uncertainty related to the jurisdictional treatment of IRECPs under Title VII, two elements of the security-based swap ("SBS") definition seem particularly relevant:

> 1) Whether an underlying event or performance metric related to a security represents an interest in a security, and
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> 2) Whether an event relating to a single issuer directly affects the financial statements, financial condition, or financial obligations of the issuer such that an option based on it would be an SBS rather than a swap.

Thesis addresses specific questions raised in the Joint RFC relating to the SBS definition in detail below. As an initial matter, Thesis notes that these current jurisdictional questions in many ways resemble historical analogues from the 1970s and 1980s. The jurisdictional uncertainty at that time was initially driven by the introduction of financial futures on exempt securities and led to the Shad-Johnson Accord. An important lesson of Shad-Johnson is that the Commissions generally do not have the ability to change Congressionally drawn jurisdictional lines between the two agencies without specific Congressional authorization.

The question of whether and when an issuer-related event or performance metric can represent an interest in a security is a fundamental definitional issue that cuts across different securities-related product definitions and predates Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Title VII").[1] In considering rules that would further define Title VII terms that incorporate the concept of an interest in a security, Thesis believes the agencies should carefully consider the broader context of any proposed changes in light of other securities definitions where those terms are used. Thesis notes that, in the agencies' joint 2012 rulemaking further defining the definitions of "swap" and "security-based swap," among other things ("Joint Definitions Rule"),[2] the agencies did not elect to further define the option on a security exclusion from the SBS definition, just as they did not elect to further define the future exclusion from the swap definition.

While Thesis recognizes that this can create overlap between classes of products such as options on securities and SBS, as well as swaps and futures, Thesis also believes the overlap allows market participants to bring innovative products to markets within appropriate, robust, regulatory regimes based on what makes sense from an investor and commercial perspective. One national securities exchange ("NSE") might seek to offer an option on an interest in a security as a traditional security derivative, but another NSE or a Security-based Swap Execution Facility might seek to offer it as an SBS. Both of these

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203 (July 21, 2010).
[2] Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 FR 48208 (Aug. 13, 2012).

could be viable pathways for listing these products so long as all applicable legal and regulatory requirements are met, based on the overlap between different product definitions.

As the Commissions consider action in this area, Thesis encourages the Commissions to provide, where appropriate, clear, and practicable guidance on how to distinguish the appropriate treatment of IRECPs jurisdictionally. Thesis believes a substantial amount of market uncertainty could be addressed through joint agency guidance on the applicability of existing definitions to IRECPs, rather than rulemaking, which could take significant time, during which uncertainty would likely continue.

Thesis addresses specific questions posed by the agencies below.

III. Responses to Specific Questions

3. Similarly, is there a need for greater clarity regarding the definitional lines between swaps, SBS, and mixed swaps? Is there a need for greater clarity regarding the scope and application of the SBS NBSI Prong, the SBS Single Security Prong, and/or the SBS Event Contract Prong?

4. Is there a need for greater clarity regarding when a swap, option (including any put, call, straddle, option, or privilege), or future is based on "any interest" in a security or group or index of securities, particularly when the swap, option, or future is not based on the value of that security or group or index of securities?

6. Regarding the SBS Single Security Prong, is additional clarity necessary regarding when a swap is based on "a single security or loan, including any interest therein or on the value thereof"? Should the Commissions further address the circumstances when a swap does or does not satisfy the SBS Single Security Prong?

> *Thesis Response*: The question of whether and when an issuer-related event can represent an interest in a security is a fundamental definitional issue that predates Title VII. Thesis believes that guidance on when an issuer-related event or performance metric can be an interest in a security would be helpful to securities derivatives and Title VII product analyses. Under Title VII, an option on an interest in a security is excluded from the SBS definition. In carving out options on an interest in a security from the SBS definition, Congress used the language that had long defined an option on a security under the SEA.
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> In issuing the Joint Definitions Rule, the agencies did not elect to further define the option on a security exclusion from the SBS definition, just as they did not elect to further define the future exclusion from the swap definition. While Thesis recognizes that this can create overlap between classes of products such as options on securities and SBS, as well as swaps and futures, Thesis believes the overlap allows market participants to bring innovative products to market within appropriate, robust regulatory regimes based on what makes sense from an investor and commercial perspective. Because one market participant might treat an option on an interest in a security as a traditional security option does not mean that another could not treat it as an SBS, given the overlapping definitions.

7. Regarding the SBS Event Contract Prong, is additional clarity necessary regarding when an event "directly affects" the financial statements, financial condition, or financial obligations of an issuer? Should the Commissions further address the circumstances when a swap does or does not satisfy the SBS Event Contract Prong? How should any further clarifications relate to the Commissions' rules and guidance on credit default swaps in the Product Definitions Adopting Release, and should such rules and guidance be revised or clarified?

> *Thesis Response*: A review of the history of Title VII and the Joint Definitions Rule suggests that a primary focus of both efforts was ensuring credit default swaps ("CDS") were regulated appropriately (Title VII) and clarifying their regulatory treatment (Joint Definitions Rule). CDS were one of the relatively few IRECPs in existence at the time of Title VII, so it is not surprising the Joint Definitions Rule focused on them. Thesis sees little evidence in the history or language of Title VII or the Joint Definitions Rule that Congress or the agencies intended to use CDS as a template for the treatment of all IRECPs, which can vary considerably. Consequently, Thesis believes the agencies' efforts may be best focused on providing clear and practicable guidance about the meaning of "directly affects the financial statements, financial condition, or financial obligations of an issuer" in the context of the SBS Event Contract Prong.
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> A wide variety of events and reporting of financial metrics *can* affect the valuation and market views on the future performance and valuation of an issuer. Typically, interest in trading products on those events or financial metrics reflects the degree of value investors see in trading those products as a proxy for some measure that investors believe is relevant to the performance and/or valuation of the issuer. Whether or not the occurrence of an event or reporting of a performance metric *actually* affects the financial statements, financial condition, or financial obligations of an issuer may only be known in hindsight.
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> One potential framework for determining whether or not an event "directly affects" the financial statements, financial condition, or financial obligations of an issuer may be whether or not a reasonable investor would view the occurrence or non-occurrence of an event, including the reporting of a financial metric, as having the potential to impact the financial statements, financial condition, or financial obligations of an issuer and/or the price of its issued securities. To avoid the test being overbroad, the Commissions could also clarify, through guidance and/or rules, what types of issuer-related events or measures would not be expected to "directly affect" the financial statements, financial condition, or financial obligations of an issuer. Thesis appreciates that line drawing is difficult here given the ambiguity of the terms involved and the potential interplay of the SBS single security prong and the SBS event contract prong. As discussed below, a joint CFTC and SEC regulatory framework allowing for an appropriate subset of CFTC and SEC jurisdictional event contracts to trade on the same platform may also be a solution.

9. Any note, bond, or evidence of indebtedness that is a security as defined in section 2(a)(1) of the Securities Act is excluded from the "swap" definition. In light of innovative products and product structures, but mindful of the existing structured notes market, is there a need to further clarify whether a particular instrument is a note, bond, or evidence of indebtedness that is a security, and thus excluded from the definition of "swap" pursuant to CEA section 1a(47)(B)(vii), as compared to a swap or SBS? For example, what consideration should be given to whether the financial instrument is issued pursuant to an indenture qualified under the Trust Indenture Act of 1939? What consideration should be given to

whether the terms of the instrument reflect a lender-borrower relationship? Are there different or additional criteria relevant to distinguishing notes, bonds, and other evidence of indebtedness that are securities from swaps or SBS?

> *Thesis Response*: Thesis does not have a view on the substance of when a product satisfies the note, bond, or evidence of indebtedness exclusion from the swap definition. However, Thesis believes that products relying on the exclusion should be labeled and marketed in a way that they are distinguishable from cash versions of related products. For instance, a tokenized equity that does not offer ownership of the underlying equity should not be called a tokenized stock, as that could be misleading to investors. Instead, if such a product is structured as a note that can satisfy the exclusion, it should be marketed as a note.

12. Where trading in economically related or functionally similar product classes implicates both SEC and CFTC regulatory interests, are there circumstances in which compliance with one Commission's regulatory framework could appropriately satisfy substantially similar requirements of the other Commission (alternative compliance)? In this case, how should "substantially similar" be viewed? Should it contemplate scope, objectives and/or outcomes of requirements? Supervisory compliance programs? Enforcement authority? Other considerations/standards?

13. Title VII provides that the Commissions may adopt rules to further define terms included in Title VII, but it also limits the exemptive authority of each Commission over certain provisions related to swaps and SBS. In light of these provisions, under what circumstances should the Commissions consider/pursue joint or coordinated notice registration, tailored rules, rules of procedure, tailored trade reporting rules, deemed filing, or other joint or coordinated approaches to facilitate alternative compliance?

14. What considerations should guide surveillance, examination, and enforcement under an alternative compliance approach? How could enhanced sharing of information and data help fulfil the Commissions' regulatory mandates under an alternative compliance approach? How could the Commissions more effectively coordinate to examine and enforce their regulatory requirements?

> *Thesis Response*: There is a long history in U.S. financial markets of clearinghouses being registered with the CFTC and SEC, as well as intermediaries being registered as both broker dealers and futures commission merchants, where necessary to support cross-jurisdictional activities. To prevent regulatory arbitrage, the general approach has been to use a "higher of" approach in observing regulatory requirements that differ across the two agencies' statutes and regulations. Thesis believes the agencies could work together to provide necessary and appropriate relief to allow certain products to trade across jurisdictional boundaries. As the agencies cannot unilaterally grant each other authority to offer non-jurisdictional products, except in limited circumstances where they are specifically authorized by Congress, Thesis believes that cross-jurisdictional trading will typically consist of some type of joint regulation with appropriate relief and conditions to address duplicative or conflicting requirements, as well as guard against regulatory arbitrage.
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> Thesis recognizes that Congress limited the agencies' exemptive authorities related to swaps and SBS, as noted in question 13. However, Congress also provided authority for swaps to trade on designated contract markets ("DCM") and SBS to trade on national securities exchanges.

Title VII does not restrict the agencies' ability to issue exemptive relief from DCM and NSE registration requirements. Thesis believes this gives the agencies latitude to consider joint regulatory frameworks with tailored relief to address duplicative and conflicting regulatory requirements. In considering this, Thesis believes the Commissions should be guided by the overall goal of ensuring economically similar products receive similar regulatory treatment.

Thesis believes event contract markets may be amenable to such an approach. The financial markets version of "Everything Everywhere All at Once" would be a difficult endeavor to pull off. Starting with a defined subset of contracts, such as event contracts, where markets are still relatively nascent and there is regulatory uncertainty, would provide a narrower scope within which to consider jointly regulated platforms that could trade both CFTC and SEC jurisdictional event contracts. An approach that facilitates jointly regulated platforms, with appropriate tailoring of requirements to address duplicative, conflicting, or inappropriately burdensome requirements, would allow the creation of a platform that could potentially list in-scope event contracts, whether they are futures, options on securities, swaps, or SBS. Thesis recognizes this would not be easy, but the task would be simplified by focusing on event contracts as a novel asset class, which could be appropriate for trading on such platforms as a starting point for consideration.

As the Commissions are aware, while Congress approved the trading of swaps and SBS on DCMs and NSEs, Congress offered little guidance as to what regulatory standards should apply. With respect to IRECPs that could be SBS, bringing these contracts to market is hampered by the low *de minimis* threshold for security-based swap dealer ("SBSD") registration. Recognizing the robust regulatory regime that exists for products traded on NSEs, Thesis believes one area where the Commissions should consider guidance, relief, or rulemaking, as applicable, is allowing SBS that trade on NSEs and are cleared by a clearing agency to either be treated as standardized options on securities or to be treated as SBS but be exempted from SBSD counting requirements. Under this approach, SBS would still be subject to robust regulatory requirements at both the exchange and intermediary levels, ensuring customer and investor protection. Smoothing the integration of SBS into NSE architecture could significantly facilitate the trading of IRECPs that are SBS.

15. Under an alternative compliance regime, how could the Commissions best deter market manipulation and trading on material non-public information? What steps should the agencies take to ensure robust surveillance and oversight of cross-market activities?

Thesis Response: Thesis commends the agencies for raising the issue of cross-market surveillance. Currently, DCMs' and NSEs' ability to conduct cross-market surveillance is limited. Exchanges generally conduct market surveillance at the exchange level and if they identify issues through their alerts and screens, they can request further information from trading venues through the Intermarket Surveillance Group ("ISG"), if they are members. The CFTC has broad authority to collect order book data from DCMs and data from market participants to conduct cross-market monitoring. The SEC, NSEs, and FINRA have access to Consolidated Audit Trail data to conduct market monitoring and surveillance. While the pieces exist for cross-market monitoring, it is made challenging by the difficulty in combining datasets across different regulatory regimes. There are no easy answers to solving this, but Thesis believes a starting point would be for the agencies, in conjunction with SROs and market participants, to develop a framework for potential harmonization of data requirements to better facilitate cross-market and cross-jurisdictional monitoring activities.

IV. Conclusion

Thesis appreciates the Commissions' attention to these related proceedings and welcomes the opportunity to discuss these comments further with Commission staff.

Respectfully submitted,

/s/ *DJ Adams*

DJ Adams
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Thesis Market, Inc.