MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

December 19, 2014

Via Electronic Submission: rule-comments@sec.gov

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-06-11: Proposed Rule and Proposed Interpretation on Registration and Regulation of Security-Based Swap Execution Facilities (RIN 3235-AK93): Supplemental Comments to MFA Letter dated April 4, 2011 and Conference Call with Staff on June 12, 2014 Relating to Updated MFA Recommendations

Dear Mr. Fields:

Managed Funds Association ("**MFA**")[1] is providing the Securities and Exchange Commission (the "**Commission**" or "**SEC**") with additional and updated comments to supplement MFA's comment letter dated April 4, 2011 ("**Prior SB SEF Letter**")[2] and MFA's June 12, 2014 conference call with staff of the SEC's Division of Trading and Markets.[3] MFA's Prior SB SEF Letter addressed the SEC's proposed rule and proposed interpretation relating to "Registration and Regulation of Security-Based Swap Execution Facilities" (the "**Proposed Rules**")[4] under Title VII[5] of the Dodd-Frank Wall Street Reform and Consumer Protection Act

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1 Managed Funds Association represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent and fair capital markets. MFA, based in Washington, DC, is an advocacy, education and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, the Americas, Australia and many other regions where MFA members are market participants.

2 *See* MFA's Prior SB SEF Letter, available at: https://www.sec.gov/comments/s7-06-11/s70611-39.pdf.

3 *See* Commission Memorandum, dated June 13, 2014, available at: https://www.sec.gov/comments/s7-06-11/s70611-152.pdf.

4 Commission Proposed Rule; Proposed Interpretation on "Registration and Regulation of Security-Based Swap Execution Facilities", Release No. 34-63825, File No. S7-06-11, RIN 3235-AK93, 76 Fed. Reg. 10948, at

(the "**Dodd-Frank Act**").[6] MFA strongly supports the Dodd-Frank Act's goal of moving trading of liquid, standardized, cleared swaps and security-based swaps ("**SB swaps**") onto registered swap execution facilities ("**SEFs**") and security-based swap execution facilities ("**SB SEFs**") that provide open and impartial access and facilitate the emergence of an "all-to-all" market (where multiple market participants meet and transact with multiple market participants).

Since the submission of MFA's Prior SB SEF Letter, the Commodity Futures Trading Commission ("**CFTC**") has adopted and implemented, and market participants have begun trading swaps pursuant to, the final rules on the registration and regulation of SEFs,[7] the trade execution requirement, the process for making swaps "available to trade"[8] and the procedures to establish appropriate minimum block sizes.[9] The CFTC has also adopted a final rule on straight-through processing ("**STP**") of cleared swaps,[10] which we believe is a fundamental prerequisite to the successful evolution of an open, competitive, all-to-all market on SEFs and SB SEFs. These final rules, together with related CFTC staff guidance[11] and related no-action relief[12] are collectively referred to herein as the "**CFTC SEF Legal Standards"**.

We are providing supplemental comments and updated recommendations to the Commission based on MFA members' SEF trading experiences to date under the CFTC's SEF

10954 (Feb. 28, 2011) ("**Proposing Release**"), available at: https://www.sec.gov/rules/proposed/2011/34-63825fr.pdf.

5 Entitled "The Wall Street Transparency and Accountability Act".

6 Pub. L. 111-203, 124 Stat. 1376 (2010).

7 *See* CFTC Final Rule on "Core Principles and Other Requirements for Swap Execution Facilities", 78 Fed. Reg. 33476 (June 4, 2013) (the "**SEF Core Principles Rule**").

8 *See* CFTC Final Rule on "Process for a Designated Contract Market or Swap Execution Facility To Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act", 78 Fed. Reg. 33606 (June 4, 2013).

9 *See* CFTC Final Rule on "Procedures to Establish Appropriate Minimum Block Sizes for Large Off-Facility Swaps and Block Trades", 78 Fed. Reg. 32866 (May 31, 2013).

10 *See* CFTC Final Rules on "Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management", 77 Fed. Reg. 21307 (Apr. 9, 2012) available at: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-7477a.pdf.

11 *See* "Division of Clearing and Risk, Division of Market Oversight and Division of Swap Dealer and Intermediary Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities", issued Nov. 14, 2013 (the "**Impartial Access Guidance**"); see *also* "Staff Guidance on Swaps Straight-Through Processing", issued Sept. 26, 2013 (the "**CFTC STP Guidance**").

12 *See* CFTC Staff No-Action Letter No. 13-66, "Time-Limited No-Action Relief for Swap Execution Facilities from Compliance with Certain Requirements of Commission Regulation 37.9(a)(2) and 37.203(a)", issued Oct. 25, 2013 ("**NAL 13-66**").

regime and the "lessons learned" through the implementation process. Further, as we expect that a number of CFTC-registered SEFs will become SEC-registered SB SEFs, we would like to ensure that a substantially uniform set of rules applies to trading swaps and SB swaps on such dually registered trading platforms to facilitate a smoother and more efficient transition to SB SEF trading. Our comments and recommendations in this letter are intended to be constructive suggestions to assist the Commission in adopting a final SB SEF rule regime that is both sufficiently harmonized with the CFTC's SEF regime, and informed by the prior experience of many MFA members with the implementation of SEF trading under that regime.

Executive Summary

In particular, in this supplemental comment letter, MFA:

- provides suggestions for the registration and regulation of dually registered SEFs/SB SEFs, such as completing the substantive review of SB SEF rulebooks before specifying the date by which market participants must comply with the SEC's first trade execution requirement for SB swaps that have been "made available to trade" ("**MAT**");

- reiterates its recommendation that the SEC remove the provision in its Proposed Rules that would allow an SB SEF to restrict access to eligible contract participants ("**ECPs**") that are not security-based swap dealers, major security-based swap participant, or brokers, as this provision would restrict buy-side market participants' access to SB SEFs in a manner inconsistent with impartial access principles;

- alerts the SEC to implicit and explicit barriers to the buy-side's impartial access to SEFs that the SEC should address in its final SB SEF rules. Such barriers have contributed to the persistence of a "two-tier" swaps market and contravene the objectives of the Dodd-Frank Act;

- explains the importance of the SEC's adoption of an STP rule to achieve a competitive, open and transparent market for SB swaps and harmonization with the CFTC and EU MiFID II STP regimes;[13]

- recommends substantial uniformity between the SEC and CFTC approaches to the trade execution requirement, but expresses support for the SEC's inclination to assume a more active role in the MAT determinations process; and

[13] *See supra* n. 10*; see also* Article 29 (*Clearing obligation for derivatives traded on regulated markets and timing of acceptance for clearing*) of the revised Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR), published in the Official Journal of the European Union on June 12, 2014, available at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.173.01.0084.01.ENG.

- recommends that the SEC adopt an approach to "package transactions"[14] that facilitates a smooth transition to trading package transactions on SB SEFs by taking a transaction-level approach for MAT determinations of package transactions that include MAT SB swaps.

I. Registration and Regulation of Dually Registered SEFs

We believe that the majority of SB SEFs will be entities that are already registered as SEFs. Many MFA members and other market participants have already expended considerable resources to onboard and connect to SEFs, including establishing connectivity, testing trading protocols and workflows, and reviewing SEF rulebooks and participation agreements, among other onboarding requirements. We are thus very concerned that we may be compelled to repeat this resource-intensive process if the SB SEF regime were materially different from the SEF regime. Substantially different or conflicting regulatory requirements would not facilitate a smooth process for existing SEFs to become dually registered SB SEFs. We thus encourage the SEC to engage with the CFTC to reach an understanding on how they will coordinate regulation of such dual registrants.

Many MFA members have experienced significant SEF onboarding challenges as a result of the CFTC's temporary registration of SEFs. While CFTC staff are undertaking an ongoing review of SEF rulebooks during the two-year period of temporary SEF registration, some buy-side firms were compelled to adhere to SEF rulebooks with provisions that are explicitly inconsistent with CFTC rules and staff guidance, in order to comply with the trade execution requirement for MAT swaps. We believe that inconsistencies with the CFTC SEF Legal Standards have been due, in part, to the CFTC's granting temporary SEF registration based only on a completeness review of SEF application documentation, pending the completion of the CFTC's substantive review of such documentation.[15] To avoid such inconsistencies and implementation challenges, we respectfully suggest that the SEC staff conduct substantive reviews of the rulebooks of all SB SEF applicants for temporary registration to ensure their compliance with the SEC's final core principles prior to the date that market participants must comply with the SEC's first trade execution requirement for SB swaps. We believe this sequencing would better serve the Dodd-Frank Act goal of promoting trading on SB SEFs.

[14] "Package transactions" are broadly defined herein as transactions involving the simultaneous and contingent execution of two or more instruments, where at least one of those instruments is a swap subject to the trade execution requirement.

[15] The CFTC noted in its final SEF rule that "it will review a SEF applicant's Form SEF to ensure that it is complete, and will not conduct any substantive review of the form before granting or denying temporary registration". *See* SEF Core Principles Rule at 33487.

II. Impartial Access Concerns

Impartial access to SEFs and SB SEFs is a cornerstone of OTC derivatives reform and is compelled by the Dodd-Frank Act.[16] We therefore urge the SEC to eliminate Proposed Rule §242.809(b) in its final SB SEF rules to achieve this statutory mandate for impartial access. Under the SEC's Proposed Rule §242.809(b), an SB SEF could restrict access to any ECPs[17] that are not registered with the Commission as a security-based swap dealer, major security-based swap participant, or broker, and prevent them from becoming participants in the SB SEF. The SEC justified such a restriction on the premise that it was seeking to strike "an appropriate balance between the statutory requirements of impartial access … and financial integrity of transactions … for SB SEFs."[18] However, with respect to cleared swaps/SB swaps that are executed on or pursuant to the rules of a SEF/SB SEF, any concern around the "financial integrity of transactions" is addressed by the participants' clearing arrangements, and thus, there is no pretext to restrict impartial access. The reason is that for SEF- (and eventually SB SEF-) executed trades, market participants who are not direct clearing members of CCPs[19] have clearing arrangements in place with their futures commission merchants ("**FCMs**")/broker-dealers to ensure that their SEF-executed trades will be cleared.

Under Proposed Rule §242.809(c)(1), such clearing arrangements would be a requirement for any eligible person to become a participant in the SB SEF.[20] In the SEF context, this arrangement includes FCMs conducting pre-execution credit checks of customer orders, which ensure that any trades that result from those orders will be accepted for clearing. Thus, the "clearance and settlement" and "counterparty credit" risks that the SEC refers to in the Proposing Release can be easily addressed.[21] The risk management controls and supervisory procedures that the SEC proposes to require of SB SEFs under §242.809(d) would further ensure the "financial integrity of transactions". As such, separately proposing to allow SB SEFs to restrict access to certain types of market participants is unjustified.

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16 *See* Dodd-Frank Act Sections 733 (SEFs) and 763(c) (adding section 3D of the Exchange Act on the registration requirements and core principles for SB SEFs) (requiring, in pertinent part, that SEFs/SB SEFs establish and enforce participation rules and have the capacity to enforce those rules, including means to provide market participants with impartial access to the market).

17 The ECP definition is contained in Section 3(a)(65) of the Securities Exchange Act of 1934, as amended (the "**Exchange Act**").

18 *See* Proposing Release at 10961.

19 The term "CCPs" refers to central counterparties that are registered with the CFTC as derivatives clearing organizations ("**DCOs**") and/or registered with the SEC as clearing agencies.

20 *See* Proposed Rule §242.809(c)(1) at 11060 (requiring in pertinent part that an SB SEF have a rule that requires a participant to "have an arrangement with a member of, a registered clearing agency to clear trades in the security-based swaps that are subject to mandatory clearing pursuant to section 3C(a)(1) of the Act (15 U.S.C. 78c-3(a)(1)) and entered into by the participant on the security-based swap execution facility").

21 *See* Proposing Release at 10961.

Further, as discussed in Section III below, to best address concerns with respect to the "financial integrity of transactions", we strongly urge the SEC to adopt an affirmative STP rule to eliminate any appreciable gap in time between trade execution and clearing. As a policy matter, we believe this solution is far preferable to the SEC's proposed authorization for SB SEFs to exercise broad discretion to restrict access to non-registered ECPs. Such discretion is unnecessary and unjustified, because an STP-compliant execution-to-clearing workflow on SB SEFs would ensure the financial integrity of SB swap transactions that are executed on SB SEFs and intended to be cleared (as it has for swaps executed on SEFs over the past year). The alternative – allowing SB SEFs to restrict access – would be prejudicial to many market participants that should be eligible to participate in the trading of SB swaps, such as MFA members, but who are not registered as SB swap dealers, major SB swap participants, or brokers.

We thus strongly believe that the SEC's Proposed Rule §242.809(b) contravenes the Dodd-Frank Act mandate of impartial access and should be eliminated. We fear that if the Commission does not eliminate Proposed Rule §242.809(b), it will be misapplied to prevent buy-side access to certain SB SEFs and contribute to the entrenchment of the current two-tier SEF market, with inter-dealer trading occurring on legacy inter-dealer broker ("**IDB**") SEFs to the exclusion of buy-side firms, and dealer-to-client trading on the dominant dealer-to-client platforms. This two-tier market could become entrenched without the SEC's vigilant regulatory oversight of SB SEFs that seek opportunities to undermine impartial access. We thus respectfully reiterate our request that the Commission's final rules should require SB SEFs to allow all ECPs to become SB SEF participants.[22] We believe this requirement would better serve the Dodd-Frank Act goal of promoting an "all-to-all" trading market on SB SEFs.

Based on our members' SEF trading experiences to date, we note that SEFs vary in their willingness to open access to the buy-side. To ensure that SB SEFs *actually* provide impartial access to their markets, we respectfully urge the SEC to consider adding provisions to its final SB SEF rules, as well as to direct SEC staff to assess the practical effects of SB SEF trading protocols and rulebook provisions. Otherwise, certain SB SEFs that prefer to exclude buy-side participants would be able to deter buy-side participation with trading protocols or rulebook provisions that, through artful construction or drafting, may appear even-handed and impartial with respect to the treatment of all participants, but would have the opposite effect.

To assist SEC staff in such assessments, we summarize below a number of implicit and explicit barriers that certain SEFs have used to block buy-side participation on their platforms, notwithstanding the impartial access mandate. We have cited these barriers as reasons for the current two-tier SEF market with the CFTC Commissioners.[23] We respectfully urge the SEC

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22 *See* MFA's Prior SB SEF Letter at p. 9. To clarify, MFA supports SEFs and SB SEFs establishing reasonable eligibility criteria for participants, including ECPs, but does not support a blanket, status-based prohibition on ECPs that are not registered SB swap dealers, major SB swap participants, or brokers.

23 *See* Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to the Hon. Timothy G. Massad, Chairman, CFTC, July 30, 2014, at 6-7, available at:

expressly to address these barriers in its SB SEF rulemaking and subsequent supervision and enforcement:

- Enablement Mechanisms: Consistent with the Impartial Access Guidance, it is our view that there is no basis for "enablement mechanisms"[24] in respect of cleared swaps on a SEF given that such enablement mechanisms undermine the emergence of all-to-all trading. There is no reason for such enablement mechanisms since transacting parties will never be exposed to each other's counterparty credit risk. Nonetheless, certain SEFs have imposed such enablement mechanisms by providing market participants with the ability to enable/disable counterparties in cleared swap markets on SEFs, or to prevent certain parties from seeing streaming prices. Eliminating such enablement mechanisms on SEFs is a necessary precondition to ensuring impartial access to SEFs for consistency with the Dodd-Frank Act.

- Express Prohibition of Breakage Agreements: We urge the SEC expressly to prohibit the applicability of so-called "breakage agreements" to trades executed on, or subject to the rules of, an SB SEF. Such breakage agreements are a type of bilateral, pre-execution enablement mechanism in which the parties address the consequences and financial exposure resulting from a swap transaction that is rejected for clearing. We believe such breakage agreements or provisions are inconsistent with the impartial access requirement under the Dodd-Frank Act, because they prevent market participants from interacting or trading with market participants who have not enabled them. For these reasons, the CFTC staff's Impartial Access Guidance prohibited the use of breakage agreements as applied to swaps executed or traded on or subject to the rules of a SEF that are intended to be cleared. Such swaps do not pose credit risk due to pre-trade credit checks and STP.

- Pre-Trade Credit Checks: Pre-trade credit checks are a prerequisite to client clearing as they remove the need for a blanket clearing guarantee. However, the willingness and operational capabilities of SEFs to enable pre-trade credit checks have varied. More specifically, some SEFs required a Participant on the SEF to represent either that it is self-clearing, or that the Participant's FCM unconditionally guarantees all of the Participant's trades. Only a dealer participant can make such a representation: (1) while certain dealers are self-

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https://www.managedfunds.org/wp-content/uploads/2014/07/MFA-Welcome-Letter-to-CFTC-Chair-Massad-Final.7.30.14.pdf. MFA also sent similar letters to each of the other CFTC Commissioners.

[24] As defined in the Impartial Access Guidance, the term "enablement mechanism" refers to any mechanism, scheme, functionality, counterparty filter, or other arrangement that prevents a participant in a SEF from interacting or trading with, or viewing the bids and offers (firm or indicative) displayed by, any other participant in such SEF. *Id*. at p. 1.

clearing, no buy-side firms are in such a position; and (2) FCMs do not provide unconditional clearing guarantees to buy-side clearing customers. Therefore, such a requirement will exclude buy-side participants from gaining access to the platform, which contravenes the Dodd-Frank Act's impartial access mandate.

- Post-Trade Name Give-ups: IDB SEFs disclose counterparty names after trade execution. This practice violates anonymity, acting as an implicit barrier to buy-side access. Anonymous order book trade execution should remain anonymous throughout the trade cycle for all participants on such SEFs. Post-trade name disclosure compromises a buy-side firm's ability to trade on an otherwise anonymous trading platform as it (i) reveals proprietary trading strategies and (ii) risks potential retaliation by liquidity providers in the still prevalent dealer-to-customer market. This barrier to buy-side access has been acknowledged by the CFTC as a practice that needs the CFTC's attention, because it is discouraging SEF trading and the use of central limit order books.[25]

- Burdensome Recordkeeping Requirements for SEF Members: Barriers to buy-side access to SEFs in the form of burdensome recordkeeping requirements under CFTC Rule 1.35(a) act as an impediment to direct access by certain CFTC-registered buy-side firms.

- Indirect Access: All SEFs and SB SEFs should have rules in their rulebooks regarding accessing their platforms through an agent or intermediary. Market participants must have the option to connect to SB SEFs indirectly, as they do in other regulated markets. Without explicit authorization of indirect or intermediated access, we believe the SEF rulebooks are inconsistent with the Dodd-Frank Act's goal to promote SEF trading in the swaps and SB swaps markets.[26]

- Pricing Schemes: Certain SEFs have pricing schemes that bar access to many buy-side firms, as pricing is only viable and affordable for certain firms to access such SEFs.

- Voice and Block Trades: We respectfully urge the SEC to ensure that its impartial access requirements for SB SEFs are applied uniformly to all SB swaps subject to the rules of an SB SEF, regardless of mode of execution, including swaps

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[25] *See infra* note 31 for citations to public remarks made by CFTC Chairman Timothy Massad and CFTC Commissioner Mark Wetjen. In Commissioner Wetjen's remarks, he noted that the CFTC should "take a careful look at the alleged information leakage resulting from post-trade affirmation services employed by SEFs." He also observed that: "It's difficult to rationalize trading protocols that reveal the identities of counterparties on an anonymous, central limit order book".

[26] *See supra* note 16.

executed by voice, block trades, as well as central limit order book and RFQ execution functionality. Based on MFA members' SEF trading experiences of swaps to date under the CFTC's SEF regime, certain dealers have attempted to apply breakage agreements to voice and block trades to inhibit all-to-all markets and provide a pretext for the use of enablement mechanisms. As discussed above, such agreements are inconsistent with the Dodd-Frank Act's impartial access mandate.

- Caps on RFQ Requests: Certain SEFs have imposed limits on the maximum number of counterparties to whom a given request for quote can be sent. This represents an enablement mechanism that limits a participant's ability to interact with other participants. The CFTC staff prohibited the use of such enablement mechanisms in its Impartial Access Guidance, because they are inconsistent with the impartial access requirement under the Dodd-Frank Act.[27]

Separately, we continue to urge the CFTC and the SEC to finalize dealer ownership restrictions or thresholds for SB SEF governance. Dealer-dominated SEFs and SB SEFs could create conflicts of interest, essentially creating a two-tiered trading market where most buy-side firms are restricted to trading on a few limited SEFs and SB SEFs.

III. Implementation of SEC STP Rule is a Linchpin to Impartial Access to SB SEFs, Optimal Risk Management, and Market Competition

We encourage the SEC to adopt a rule requiring STP of cleared SBS transactions as a fundamental prerequisite for mandatory clearing of SB swaps, and for the evolution of trading on SB SEFs.

STP benefits all market participants, especially smaller buy-side market participants and new liquidity providers that could otherwise encounter barriers to entry, in that it: (i) gives market participants certainty of clearing immediately following execution, which in turn, allows them to hedge more efficiently and effectively manage risk; (ii) is an important factor in encouraging the implementation of broad, mandatory clearing; (iii) is essential to electronic trading, particularly central limit order book trading, as it is not possible to enter into an electronic transaction on an anonymous basis without both the immediate confirmation of the execution of the transaction and its acceptance for clearing; and (iv) promotes accessible, competitive markets and access to best execution by ensuring parties to a cleared transaction have immediate confirmation that they will face the relevant clearinghouse, thus eliminating the need to negotiate individual credit arrangements with each of their counterparties, as is required in bilateral derivatives markets.

If there is any material gap in time between trade execution and clearing, counterparty credit risk is re-introduced. This counterparty credit risk narrows the universe of trading

[27] *See* Impartial Access Guidance at 2.

counterparties and re-introduces the need for negotiated credit arrangements. Thus, an affirmative STP rule is critical to a competitive, open and transparent market for SB swaps that are intended to be cleared.

The SEC would achieve harmonization with the CFTC and the EU's MiFID II regimes by adopting a parallel STP requirement. The CFTC has demonstrated its robust support for STP by issuing final rules that: (i) minimize or effectively eliminate the time between transaction execution and acceptance into clearing; and (ii) mandate STP for all transactions regardless of the mode of execution, including both those executed on a designated contract market or SEF as well as those executed outside an execution platform and submitted for clearing (*e.g.*, executed by voice).[28] CFTC staff previously interpreted "as soon as technologically practicable" to be 60 seconds with respect to the length of time a DCO had to accept (or reject) a trade for clearing, but issued more recent guidance that shortens that time frame to 10 seconds based on recent trade acceptance data from DCOs.[29] FCMs have 60 seconds to accept (or reject) a trade for clearing, though with respect to SEF-executed trades, the requisite pre-execution credit checks further shorten the execution-to-clearing workflow timeline.

Similarly, Article 29 of the MiFID II Level 1 text provides that central counterparties, trading venues and investment firms which act as clearing members are required to have in place effective systems, procedures and arrangements to ensure that transactions in cleared derivatives are submitted and accepted for clearing "as quickly as technologically practicable using automated systems". This obligation applies to derivatives which are required to be cleared under either the European Market Infrastructure Regulation ("**EMIR**") or MiFID II, and also to derivatives which the parties agree are to be cleared. The European Securities and Markets Authority ("**ESMA**") is required to develop draft regulatory technical standards to specify the minimum requirements for systems, procedures and arrangements (including the acceptance time frames) necessary to comply with Article 29.

The SEC similarly should adopt a parallel STP rule to achieve harmonization with the CFTC and EU MiFID II STP regimes and to ensure that the SB swaps market develops consistently and is afforded the same benefits.

IV. The SEC Should Retain its Approach to Applying the Trade Execution Requirement

Generally, we prefer that the regulators apply a uniform set of rules to trading swaps and SB swaps on dually registered SEFs/SB SEFs. However, one area in which we believe the SEC

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28 *See* CFTC Final Rules on "Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management", 77 Fed. Reg. 21307 (April 9, 2012), available at: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-7477a.pdf, which require the acceptance or rejection of a transaction "*as quickly as technologically practicable if fully automated systems were used*".

29 *See* CFTC STP Guidance at p.5.

should retain its proposed approach rather than to conform to the CFTC's approach is the MAT determination process. More specifically, we support the SEC's inclination to assume an active role in setting the appropriate product scope for SB swaps in MAT determinations by establishing objective measures for such determinations, rather than allowing one SB SEF or a group of SB SEFs to establish such measures.[30]

By contrast, the CFTC relied on self-certifications from SEFs for MAT determinations, which the CFTC may be revisiting.[31] This passive role hindered the CFTC's ability to reject or modify the scope of a SEF's self-certified MAT determination, even in the face of valid concerns that industry participants raised through the CFTC's public comment process on the self-certifications that initially included forward-starting and non-benchmark tenor swaps, as well as package transactions. The over-expansive scope of certain SEFs' initial MAT determinations in the rates asset class was only narrowed by their own amendments to their self-certifications.

V. Lessons Learned from MAT Determinations of Package Transactions

MFA respectfully recommends that the SEC take a transaction-level approach for MAT determinations of package transactions that include SB swaps. Both the liquidity profile, and the ability of market infrastructure to facilitate trading, of SB swaps executed on an outright basis as distinguished from SB swaps executed as part of a package transaction can vary widely. Therefore, with respect to package transactions, MAT determinations should be made at the package level, rather than at the component instrument level. Our suggestion is informed by the CFTC's MAT process rule, which requires SEFs to apply the CFTC's MAT determinations criteria at the instrument level, and the lessons learned from application of that process to package transactions, which we summarize below.

In response to the intersection of the MAT determinations and language in the CFTC's SEF Core Principles Rule that defines a "Required transaction" as "any transaction involving a swap that is subject to the trade execution requirement",[32] MFA and other trade associations, as well as a broad spectrum of market participants, submitted numerous comment letters and requests for no-action relief to the CFTC describing the legal, operational and technological

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30 *See* Proposing Release at 10969.

31 *See* Remarks of Timothy G. Massad before the Swaps Execution Facilities Conference (SEFCON IV), as prepared for delivery on November 12, 2014, at 3 (recognizing market participants' concerns with the CFTC's SEF-initiated MAT process and requests for the CFTC to assume a more active role in that process); these remarks are available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opamassad-4. S*ee also* Remarks of Commissioner Mark Wetjen before the Cumberland Lodge Financial Services Policy Summit, as prepared for delivery on November 14, at 4-5 (recommending that the CFTC should revise the MAT process as a CFTC determination, rather than the existing MAT process via SEF or DCM rule filing, to provide "needed objectivity and certainty to the marketplace" and to "better coordinate future trading mandates with other global regulators" in order to "reduce intra and inter-market fragmentation" over time); these remarks are available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/opawetjen-10.

32 *See* CFTC's SEF Core Principles Rule, § 37.9(a)(1), at 33586.

challenges they would face if the CFTC mandated SEF trading of package transactions involving a component MAT swap before the industry developed comprehensive solutions for such challenges. MFA and other commenters also advocated for an appropriate regulatory construct as a longer-term solution for the execution of such package transactions on SEFs.[33] CFTC staff responded to industry concerns by issuing a no-action letter in February 2014 that provided relief until May 15, 2014 from mandatory trading of certain swaps executed as part of package transactions.[34] The no-action relief period also provided CFTC staff with time to analyze further the technological, operational, and jurisdictional issues for mandatory trading of package transactions, including the appropriate grouping of such transactions for a phased implementation approach to the trade execution requirement.

Based on the CFTC's further analysis of industry concerns and the time needed to develop comprehensive solutions for the SEF trading challenges posed by different groups of package transactions,[35] CFTC staff provided additional no-action relief on May 1, 2014 to market participants in respect of certain package transactions, with such relief phased in between May 15, 2014 through November 15, 2014.[36] Under this phase-in timeline, the most liquid and standardized types of package transactions, such as swap curves and butterflies that are comprised exclusively of benchmark swaps, are now subject to the trade execution requirement. More complicated types of package transactions, even where some components are not yet MAT

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33 We refer the SEC to the series of comment letters filed with the CFTC located at, for example, http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1409, which, in relevant part, discuss in detail the nature and business drivers for package transactions and the challenges with which market participants would be faced once (as is now the case) the CFTC's trade execution requirement applies to MAT swaps executed as part of package transactions. We refer the SEC, in particular, to the letter to the CFTC from MFA, dated November 21, 2013, regarding Industry Filings IF 13-004, 13-005, and 13-007 (the "**MFA Letter**") and the letter to the CFTC from Citadel LLC, dated November 29, 2013 (the "**Citadel Letter")**. The MFA Letter and the Citadel Letter both recommended a phase-in of mandatory SEF trading for package transactions in order (i) to allow the market to first transition to SEF trading of outright benchmark swaps, which are the building blocks for a wide array of package transactions in the rates asset class, and (ii) to afford market participants time to resolve a number of legal, operational and technological limitations to SEF trading of package transactions. We respectfully request that the SEC view our MAT process recommendations set out in this letter in light of the comments in those letters concerning package transactions.

34 *See* CFTC No-Action Letter No. 14-12, issued February 10, 2014, available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/letter/14-12.pdf.

35 *See, e.g.*, MFA Request for Relief from the Trade Execution Requirement for Swaps Executed as Part of Package Transactions in the Interest Rate Asset Class, dated January 24, 2014, available at: https://www.managedfunds.org/wp-content/uploads/2014/01/Packaged-Transactions-NAL-Final-MFA-Letter.pdf.

36 *See* CFTC No-Action Letter No. 14-62, issued May 1, 2014, available at: http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-62.pdf.

or clearable, are now subject to extended no-action relief from CFTC staff in order to phase-in the trade execution requirement for MAT swaps executed as part of such package transactions.[37]

While a phased implementation approach is helpful to facilitate a smoother transition to mandatory SEF trading of package transactions, we believe that the real lesson learned is that the SEC should require MAT determinations for any package transaction to occur at the transaction level (*i.e.*, for the package as a whole), rather than basing such MAT determinations at the instrument level for an individual component SB swap leg that meets the SEC's MAT criteria. This approach would avoid the SEC having to resort to the use of serial no-action relief like the CFTC has had to issue.

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MFA thanks the Commission for the opportunity to provide supplemental comments regarding the Proposed Rules. Please do not hesitate to contact Laura Harper Powell or the undersigned at (202) 730-2600 with any questions the Commission or its staff might have regarding this letter.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President, Managing Director & General Counsel

cc: The Hon. Mary Jo White, Chairman
The Hon. Luis A. Aguilar, Commissioner
The Hon. Daniel M. Gallagher, Commissioner
The Hon. Michael S. Piwowar, Commissioner
The Hon. Kara M. Stein, Commissioner

Stephen Luparello, Director, Division of Trading and Markets

[37] *See* CFTC No-Action Letter No. 14-137, issued November 10, 2014, available at: http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-137.pdf.