

MEMORANDUM

TO: File No. S7-06-11 and File No. S7-27-10

FROM: Iliana Lundblad

RE: Implementation of Dodd-Frank Wall Street Reform and Consumer Protection Act

DATE: June 24, 2011

On June 23, 2011, James Brigagliano, Heather Seidel, Thomas Eady, Gregg Berman, Nancy Burke-Sanow, David Liu, John Polise, Stephanie Mumford, Tina Barry, Heidi Pilpel, Iliana Lundblad, Michael Ogershok, and Jasmin Sethi, met with representatives from Bloomberg including George Harrington (Head of Fixed-Income Trading), Greg Babyak (Government Affairs), Greg Dumark (Compliance) and Joe Zangri (Chief Compliance Officer).

The agenda for the meeting and supplemental materials are attached.

SEC/Bloomberg Meeting

Agenda - Thursday, June 23, 2011 (10:00 a.m.)

- I. Non-Block RFQ Trades Interacting with Resting Bids and Offers
- II. Block Trades Interacting with Resting Bids and Offers
- III. SB SEF Proposed Governance and Financial Disclosure Requirements. See Addendum A

Bloomberg L.P.'s Position: Proposed Governance and Financial Disclosure Requirements:

I. Background:

The Securities and Exchange Commission ("Commission") has proposed rules to mitigate conflicts of interest in the operation of a security-based swap ("SB swap") execution facility ("SB SEF") under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or "Act").¹ Specifically, the proposed rules seek to address conflicts of interest arising from the control of market facilities, including SB SEFs, by certain OTC derivative market participants. The Commission's concern relates, in part, to the OTC derivatives market being "dominated by a small number of banks."² The structural governance proposal includes a requirement that a SB SEF Board of Directors be composed of a majority of independent directors.³

Separately, the Commission is proposing to require an applicant for SB SEF registration to provide a complete set of unconsolidated financial statements (for the latest two fiscal years) of any affiliated entity that owns, directly or indirectly, a 25% interest in the SB SEF.⁴ The Commission seeks to obtain such information on the basis that the financial health of affiliated entities could potentially have an impact on the financial condition of a SB SEF.

II. Bloomberg's Position:

Congress did not require the Commission to adopt rules mitigating conflicts of interest with respect to entities not specified in Section 765 of Dodd-Frank.⁵ In addition, even with respect to specified entities, rules to mitigate conflicts shall be adopted only after the Commission conducts a review to

¹ *Ownership Limitations and Governance Requirements for Security-Based Swap Clearing Agencies, Security-Based Swap Execution Facilities and National Securities Exchanges with Respect to Security-Based Swaps under Regulation MC*, 75 FR 65882, 65887 (Oct. 26, 2010) ("Regulation MC Release").

² *Id.* at 65887. "Derivatives activity in the U.S. banking system continues to be dominated by a small group of large financial institutions. Five large banks represent 97% of the total banking industry notional amounts . . .", noted the Commission citing an Office of the Comptroller of the Currency report.

³ The Commission also proposes to require that a SB SEF have a Nominating Committee composed of a majority of independent directors to administer the process of nominating individuals as independent directors of the Board.

⁴ *Registration and Regulation of Security-Based Swap Execution Facilities*, 76 FR 10948, 11069 (February 28, 2011) .

⁵ The market participants specified in Section 765 of Dodd-Frank are, generally, bank holding companies with \$50 billion or more in total consolidated assets, a nonbank financial company supervised by the Board of Governors of the Federal Reserve System, an affiliate of such bank holding company or nonbank financial company, a security-based swap dealer or a major security-based swap participant.

determine whether such rules are "necessary and appropriate."⁶ A wholesale application of the proposed governance requirements to SB SEFs that are not owned by the entities that gave rise to Congress's concern (e.g., specified entities) is not supported by Dodd-Frank and would be unnecessarily restrictive. The very type of entities that should be encouraged to act as a SB SEF, entities that are independently owned and not controlled by specified entities, would be discouraged from registering as a SB SEF under the current proposal. The current proposal would require a SB SEF to cede control of its Board to a majority of independent directors. Ceding Board control for an independent, privately-held company seeking to register as a SB SEF where there is no ownership structure that would give rise to the Dodd-Frank conflict of interest concerns inappropriately forces a restrictive governance model on an entity already "unaffiliated" with market participants and pushes such entity to the sidelines. This cannot be what Congress intended.

We believe the Commission should remove the proposed governance requirements from Regulation MC where an entity is not owned by the "specified entities." Alternatively, as previously commented, we believe that where a SB SEF is not owned by its members or other market participants and where the SB SEF can demonstrate a sufficient mitigation of potential conflicts of interest, the Commission should consider exempting a SB SEF from proposed governance provisions of Regulation MC.

Similarly, we believe that the Commission's proposed requirement to provide financial statements for affiliated entity of a SB SEF is an unreasonable and overly burdensome requirement without justification. As proposed, a SB SEF is required to have financial resources to cover its operating costs for a one-year period, as calculated on a rolling basis.⁷ We believe that where an affiliate does not exercise day-to-day control over a SB SEF and the SB SEF is independently sufficiently capitalized, there is no need to look to the financial health of an affiliate.

⁶ Section 765(b) of Dodd-Frank.

⁷ See Proposed Rule 821. 76 FR 10948, 11064.