

June 10, 2022

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

Re: Rules Relating to Security-Based Swap Execution and Registration and Regulation of
Security-Based Swap Execution Facilities (File No. S7-14-22)

Dear Ms. Countryman:

The Investment Company Institute¹ is writing to respond to the Securities and Exchange Commission's ("Commission") rule proposal related to the registration and regulation of security-based swap execution facilities (SBSEFs).² The Proposal seeks to closely harmonize a proposed regulatory regime for SBSEFs³ with analogous Commodity Futures Trading Commission (CFTC) rules for swap execution facilities (SEFs) in most instances, as the Commission correctly believes that the entities most likely to register as SBSEFs are those already registered with the CFTC as SEFs. We commend the Commission for seeking to harmonize its regulatory approach with that of the CFTC⁴ and agree that such alignment, subject

¹ The [Investment Company Institute](http://www.ici.org) (ICI) is the leading association representing regulated investment funds. ICI's mission is to strengthen the foundation of the asset management industry for the ultimate benefit of the long-term individual investor. Its members include mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and UCITS and similar funds offered to investors in Europe, Asia, and other jurisdictions. Its members manage total assets of \$29.7 trillion in the United States, serving more than 100 million investors, and an additional \$9.3 trillion in assets outside the United States. ICI has offices in Washington, DC, Brussels, London, and Hong Kong and carries out its international work through [ICI Global](http://www.ici.org/global).

² *Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities*, Exchange Act Release No. 34-94615 (April 6, 2022), 87 Fed. Reg. 28872 (May 11, 2022) ("Proposing Release" or "Proposal"), available at <https://www.govinfo.gov/content/pkg/FR-2022-05-11/pdf/2022-07850.pdf>.

³ Our comments with respect to the proposed rules for SBSEFs also apply to security-based swap exchanges to the extent applicable ("SB swap exchanges").

⁴ ICI provided substantive comments to the CFTC as it developed the regulatory framework for SEFs, providing recommendations to, among other things: enhance the processes to determine which swaps must be traded on a SEF and when a swap should no longer be required to trade on a SEF; modify the compliance and implementation schedules for the final rules for SEFs to facilitate an efficient transformation of the swap markets; and retain and improve certain SEF trading practices. Our recommendations on the Proposal are largely based on that experience. See e.g., Letter from David Blass, General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC (Aug. 17, 2015), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=27740>.

to our recommended modifications, will facilitate efficiencies for market participants, many of whom have already developed systems, policies, and procedures to comply with the CFTC's regulatory framework for SEFs. Among other aspects, we support the Commission's proposed prohibition of post-trade name give-up,⁵ as well as the impartial access requirements for SBSEFs.⁶ Our members have found that such rules have improved competition, fairness, liquidity, and efficiency in the swap markets. We anticipate the same benefits will result in the SB swap markets if the Commission adopts analogous rules for the SBSEF regime.

Notwithstanding our support, we recommend that the Commission take a sequential approach to implementing the SBSEF framework by clarifying that only SB swaps subject to mandatory clearing will be eligible for "made available to trade" (MAT) determinations. We also offer several recommendations to strengthen the proposed MAT determination process, which largely mirrors the CFTC's existing process. In brief, we recommend that the Commission:

- enhance and mandate consideration of all MAT factors, and establish a robust process and standards for determining that an SB swap is no longer available to trade;
- establish a 30-day public comment period for all proposed MAT determinations and provide a compliance period of at least 90 days for implementation; and
- create an advisory board to help facilitate the process.

We also provide recommendations on aspects of the proposed methods of execution for required transactions, including the exception for block trades, and request guidance on the use of pre-execution communications. Additionally, we provide a recommendation on the cross-border application of the Commission's proposed framework. We discuss these recommendations further below.

⁵ See Proposing Release at 28897 (Proposed Rule 815(f)). ICI previously supported an analogous CFTC proposal to prohibit post-trade name give up for swaps that are executed anonymously on SEFs and that are intended to be cleared. See Letter from Sarah Bessin, Associate General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC (Mar. 2, 2020), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=29092>.

⁶ We have previously noted that, based on our members' experience with CFTC-registered SEFs, some trading platforms in institutional markets seek to limit membership to certain classes of market participants, such as bank SB swap dealers. The proposed impartial access requirements would help ensure that investment advisers to regulated funds will be able to participate in these markets, accessing the pricing and other market information that may be available on SBSEFs, which would increase transparency in the derivatives market. Such requirements will also allow a broad range of market participants to transact on SBSEFs, which may lead to new participants, such as electronic market makers, entering the SB swap markets. Letter from Susan Olson, General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC (Mar. 12, 2019), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=28855>.

I. Background

US-registered investment companies, including mutual funds, ETFs and other funds that are regulated under the Investment Company Act of 1940 (“registered funds”), and non-US regulated funds (together with registered funds, “regulated funds” or “funds”) rely on their investment adviser to invest fund assets and implement their investment objectives and strategies. Fund advisers use a variety of different instruments, including SB swaps, to manage funds’ investment portfolios. For example, a portfolio manager may use SB swaps to hedge a regulated fund’s positions, equitize the regulated fund’s cash that it cannot immediately invest in direct equity holdings, manage the regulated fund’s cash positions, and adjust portfolio duration, all in accordance with the investment objectives stated in the fund’s prospectus.

ICI and its members have a strong interest in the regulation of SBSEFs and their trading practices. ICI members currently utilize CFTC-registered SEFs for trading of interest rate swaps and credit default swaps (CDS) and will likely use SBSEFs to execute SB swaps on behalf of their fund clients. These SB swaps will likely include those that become subject to the proposed trade execution requirement (*i.e.*, are required to trade on or subject to the rules of an SBSEF)⁷ as well as SB swaps that ICI members may voluntarily choose to execute through an SBSEF.

II. The Commission Should Take a Sequential Approach in Implementing the SBSEF Framework

ICI strongly recommends that the Commission clarify that the scope of eligible SB swaps for a MAT determination is limited to only those that have already been determined to be subject to mandatory clearing. The Commission itself acknowledges that the “benefits and costs associated with the trade execution requirement would not materialize unless and until the Commission makes mandatory clearing determinations.”⁸ As proposed, however, an SB swap transaction must be executed on an SBSEF upon the later of: (1) 30 days after a MAT determination for that SB swap is approved or certified; and (2) a determination by the Commission that the SB swap is required to be cleared under Section 3C(a) of the Securities Exchange Act of 1934 (“Exchange Act”), or any later compliance date that the Commission establishes as a term or condition of such determination, or following a stay and review of such determination. This suggests that a clearing determination for an SB swap could occur after a MAT determination.

Our recommended sequential approach would harmonize the Commission’s approach with that of the CFTC, which has explicitly stated that it will *only* review MAT submissions for swaps that are already subject to a clearing requirement. The CFTC viewed this approach as consistent with

⁷ See Proposed Rule 816.

⁸ Proposing Release at 28947. The Commission similarly states that proposed Rule 816 “would establish procedures for an SBSEF to make an SBS available to trade (*assuming it is also subject to the clearing requirement*), thereby activating the trade execution requirement with respect to that SBS.” *Id.* at 28898 (emphasis added).

the statutory trade execution requirement under the Commodity Exchange Act.⁹ Given that Section 3C of the Exchange Act includes identical language with respect to SB swaps, we believe that the Commission should adopt the same approach.¹⁰

Identifying the products that must be cleared first would benefit market participants by signaling that they may need to onboard to an SBSEF and trade certain SB swaps through prescribed methods of execution. It would also help to focus the assessment of which SB swaps would be liquid enough for trading on an SBSEF. Absent a prior clearing determination, a MAT determination would not provide market participants with legal and operational certainty. The lack of a prior clearing determination also may disincentivize market participants from providing meaningful public comment regarding a proposed MAT determination, as there would remain significant uncertainty about the likelihood of the SB swap ultimately becoming subject to mandatory execution. Further, we believe that a sequential approach would also avoid potential delays to implementing the overall SBSEF framework.

III. The Commission Should Not Mirror the CFTC's Approach to the MAT Process

We urge the Commission to not adopt a MAT determination process that is based on the current CFTC process. Unfortunately, the Commission proposes a mechanism for MAT determinations for SB swaps that is virtually identical to the CFTC's MAT process for swaps. The implications of an SB swap being "made available to trade" are significant, given that such an SB swap could *only* be traded on an SBSEF through prescribed methods of execution (*i.e.*, an order book or RFQ system) that are intended to increase pre-trade transparency. While we support the goals of promoting pre-trade transparency, we emphasize that a process that does not properly assess liquidity would be disruptive to the SB swap market, which is smaller than other swap markets.¹¹

ICI as well as other commenters have consistently expressed concerns about the CFTC's existing MAT process for interest rate swaps and credit default swaps.¹² Most recently, the Market Structure Subcommittee of the CFTC's Market Risk Advisory Committee issued a report

⁹ See *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, 33609 (June 4, 2013), available at <https://www.govinfo.gov/content/pkg/FR-2013-06-04/pdf/2013-12250.pdf>.

¹⁰ Based on this approach, the initial MAT determinations submitted to the CFTC in the fall of 2013 were limited to interest rate and credit default swaps that had already become subject to the clearing requirement in August 2012. This sequence was beneficial to market participants because it gave them time to transition to mandatory clearing and to assess which swaps could be subject to a MAT determination. See CFTC, Swaps Made Available to Trade Determination, <https://sirt.cftc.gov/sirt/sirt.aspx?Topic=%20SwapsMadeAvailableToTradeDetermination>.

¹¹ See Proposing Release at 28875.

¹² See, e.g., Letter from David Blass, General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC (Aug. 17, 2015), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=27740>; Letter from Karrie McMillan, General Counsel, ICI, to David A. Stawick, Secretary, CFTC (Feb. 13, 2012), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=23847>.

representing a “consensus blueprint among market participants” that recognized key concerns regarding the CFTC’s MAT process and provided several recommendations to address those concerns.¹³ Our recommendations, which we discuss below, align in significant respects with that report. While the CFTC has yet to implement reforms, it has indicated that it intends to consider recommendations to reform its MAT process.¹⁴ We strongly recommend that Commission refrain from adopting a MAT process based on the CFTC’s existing flawed process and, instead, coordinate with the CFTC as it considers potential reforms to improve its MAT process.

The concerns we have raised regarding the CFTC’s MAT process apply equally, if not more, to the Commission’s proposed MAT process because of the unique liquidity profile of the SB swap market.¹⁵ Specifically, the Commission’s proposed approach will give SBSEFs the sole ability to dictate the scope of SBSEF trading for market participants based on the commercial interests of SBSEFs.¹⁶ The Commission’s proposed factors,¹⁷ which are neither mandatory nor based on calculated thresholds, would permit SBSEFs to assert that an SB swap should be “made available to trade,” even absent objective evidence of a sufficiently liquid trading market.¹⁸ This would

¹³ Market Structure Subcommittee, Market Risk Advisory Committee of the CFTC, *Recommendations Regarding the “Made Available to Trade” (MAT) Process* (Feb. 10, 2021) (“MRAC Report”), available at https://www.cftc.gov/media/5691/MRAC_MarketStructureSubcommitteeRecommendationsRegardingtheMATProcess022321/download.

¹⁴ The most recent CFTC Regulatory Agenda lists “Amendment to the [MAT] Process” as an item in the “Proposed Rule Stage.” Agency Rule List – Fall 2021, Commodity Futures Trading Commission, available at https://www.reginfo.gov/public/do/eAgendaMain?operation=OPERATION_GET_AGENCY_RULE_LIST¤tPub=true&agencyCode=&showStage=active&agencyCd=3038&csrf_token=FB2D0B63ABE591A5E56D43F7A691990D3B89165CC662BBE40547450EB2182E2106654458BD345AEE2F4D5872C706C0A69CC9.

¹⁵ The Commission observes that the SB swap market “is a small fraction of the overall swap market.” which in turn means that the SB swap market is characterized by fewer transactions and is potentially less liquid than the swap market. As the Commission points out, the global swap market as of December 2020 had a notional amount outstanding of approximately \$571 trillion, while the global SB swap market had a notional amount outstanding of approximately \$7.1 trillion. Proposing Release at n. 371 (citing Global OTC Derivatives Market: Table D5.2 Commodity Contracts, Credit Default Swap, Bank for International Settlements (updated Jan. 13, 2022), available at <https://stats.bis.org/statx/srs/table/d5.2>).

¹⁶ The Commission’s proposed approach raises the risk that an SBSEF that is the only platform listing a particular SB swap could use the process to direct all trading of that SB swap onto its own platform.

¹⁷ Under Proposed Rule 816(b), an SBSEF “shall consider, as appropriate, the following factors: (1) whether there are ready and willing buyers and sellers; (2) the frequency or size of transactions; (3) the trading volume; (4) the number and types of market participants; (5) the bid/ask spread; or (6) the usual number of resting firm or indicative bids and offers.”

¹⁸ The proposed rules provide that an SBSEF must submit MAT determinations for SB swaps to the Commission, either for approval or self-certification. The SBSEF’s filing would be required to include, among other things, an explanation and analysis of its consideration, as appropriate, of the factors set out in the proposed rules. However,

have negative consequences for buy-side participants such as funds—requiring SB swaps with insufficient liquidity to be traded via an order book or an RFQ system would raise a significant risk of revealing advisers’ sensitive portfolio management strategies. Such information leakage could lead to front-running of funds’ trades and to other abusive trading practices that would negatively affect the pricing of SB swaps and of other related instruments, resulting in higher investment costs for adviser’s clients, including funds and their investors.

A. The Commission Must Enhance its Authority Over the MAT Determination Process

We recommend that the Commission enhance its oversight over the MAT process by ensuring that it has a more meaningful ability to review and reject MAT determinations, as well as the ability to initiate determinations itself as appropriate. As proposed, if concerns about a particular MAT determination were raised, the Commission would not have adequate time to consider, or authority to challenge, the basis for the determination. The Commission could only reject a determination if the Commission finds it to be “inconsistent with the [Exchange] Act or the Commission’s rules thereunder.”¹⁹ Without requiring an SBSEF to consider *any* objective factors (*e.g.*, threshold liquidity levels), however, it is not clear how the Commission could ever find that a MAT determination is inconsistent with the Exchange Act or the Commission’s rules.²⁰ The Commission’s limited role is concerning, given the potential conflict of interest SBSEFs face when submitting determinations for approval or self-certification.

To most effectively strengthen its authority, the Commission should enhance the MAT determination factors by:

- Clarifying that all factors must be evaluated, rather than just one or a subset;
- Adding as a factor the number of SBSEFs that list the SB swap as a factor, and requiring that at least two SBSEFs list the SB swap; and
- Requiring a minimum amount of trading history (*e.g.*, that an SB swap has been listed for at least 90 days).

the Commission does not provide any further guidance or standards as to the depth and level of such review, or the nature of the required explanation or analysis.

¹⁹ See Proposed Rules 806(b) and 807(c)(3).

²⁰ The proposed rules further result in a fundamental contradiction in the applicability of MAT determinations, which is also present in the CFTC’s MAT rules, and which we believe the Commission should address before adopting any MAT process. Specifically, the Proposal suggests that a “rule” made or issued by an SBSEF, including a MAT determination, would only be applicable to that SBSEF and its participants or members. Proposed Rules 802, 816(a)(1). Under the Proposal, however, a MAT determination that is approved or certified would affect the participants of *all* SBSEFs by limiting the methods of execution for the applicable SB swap on those SBSEFs and prohibit them from executing OTC trades in the applicable SB swap. See Proposed Rule 816(c).

The Commission should make the MAT determination factors more robust by establishing at least some objective mandatory criteria. Doing so would provide the Commission with greater authority to reject a MAT determination given the narrow standard of review for “rules” filed with the Commission for approval or self-certification.²¹ Likewise, the Commission should require that consideration of each factor be mandatory and require a demonstration of consistent trading over time across multiple SBSEFs. These requirements would address the conflict raised by an SBSEF’s commercial incentive to make an SB swap available to trade, as well as ensure that there is enough liquidity in an SB swap before it is subject to a MAT determination. A more robust MAT determination process is critical to bring consistency to the SB swap market over time, as having objective standards would avoid MAT determinations based on subjective assessments of liquidity that may change over time.

B. The Commission Should Provide for an Adequate Opportunity for Public Comment on MAT Determinations

We recommend that the Commission require a 30-day public comment period for all MAT determinations.²² Under the Proposal, it would be possible for a MAT determination to become effective without an opportunity for public comment.²³ Further, the MAT process would be controlled almost entirely by one segment of the SB swap markets—SBSEFs. Even if the Commission allows for greater Commission input into the process, SBSEFs will likely continue to play a primary role. Market participants provide the Commission with invaluable commentary, insights, and data on the potential effects of proposed rules, as well as help to ensure that rules are implemented in a fair and orderly manner.²⁴ Because MAT determinations are data intensive, 30 days would give market participants sufficient time to analyze the data presented by the SBSEF, prepare their own data and analyses, and comment effectively on operational and

²¹ Establishing objective mandatory criteria would give the Commission a more concrete basis with which to find that a MAT determination is “inconsistent with” the Exchange Act or the Commission’s rules thereunder. *See supra* at 6.

²² This would ensure there is consistency between the MAT determination process and the Commission’s process for review of mandatory clearing determinations, which includes a 30-day public comment period. *See* 15 U.S.C. 78c–3(b).

²³ The proposed approval procedure does not require any comment period. *See* Proposed Rule 806. The proposed self-certification procedure only provides for a public comment period if the Commission elects to stay the determination for an additional 90-day period. *See* Proposed Rule 807. If the Commission does not issue a stay, it would be possible for a proposed MAT determination submitted pursuant to the self-certification procedure to become effective in 10 business days without any public comment.

²⁴ With respect to the CFTC, the importance of the public comment period for MAT determinations was demonstrated by a SEF’s decision in 2013 to amend its initial, overly broad MAT submission in response to public comment on the initial submission. *See* Letter from David Blass, General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC, at 5-6 (Aug. 17, 2015), *available at* <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=27740> (discussing Javelin SEF, LLC’s MAT submission and how Javelin amended its MAT determination in response to extensive public criticism).

technological implications.²⁵

C. The Commission Should Provide Adequate Time Before a MAT Determination Becomes Effective

The Commission should provide market participants with adequate time following a final MAT determination to prepare their systems and procedures before the determination is made effective. As noted above, an SB swap transaction would need to be executed on an SBSEF upon the later of: (1) 30 days after a MAT determination for that SB swap is approved or certified; and (2) a determination by the Commission that the SB swap is required to be cleared under Section 3C(a) of the Exchange Act, or any later compliance date that the Commission establishes as a term or condition of such determination, or following a stay and review of such determination.²⁶

Consistent with the MRAC Report, we recommend that the Commission provide 90 days after a MAT determination is final before it becomes effective.²⁷ Market participants will need an adequate compliance period after a mandatory clearing determination is made *and* after the swap is first made available to trade on an SBSEF. Under the proposed approach, if an SB swap is made available to trade fewer than 30 days before a mandatory clearing determination, then that SB swap would be subject to mandatory trading on an SBSEF with a less than 30-day compliance period.²⁸ Moreover, even when an SB swap is already subject to mandatory clearing,

²⁵ To implement our recommendation, the Commission should state in the release adopting any final rules that all MAT determinations submitted for approval will be subject to an extension of the 45-day review period, which will include a 30-day comment period. Likewise, the Commission should provide assurance that all MAT determinations submitted for self-certification will be subject to a stay, which will trigger the mandatory 30-day comment period.

²⁶ As currently worded, the Proposal suggests that the Commission could make a clearing determination *after* a MAT determination is approved or deemed self-certified. As discussed above, we urge the Commission to only allow for MAT determinations with respect to SB swaps that have already been determined to be subject to the clearing requirement. *See supra* at 3-4.

²⁷ *See* MRAC Report at 3.

²⁸ For example, if a MAT determination for an SB swap is approved or certified on the first day of a month, and a clearing requirement for that SB swap is made 14 days thereafter, then the compliance date for mandatory trading on an SBSEF could potentially occur at the beginning of the following month. In that case, market participants would have less than 30 days to prepare to comply with the trade execution requirement (*i.e.*, from the time there is *both* a final MAT determination as well as a mandatory clearing determination). This assumes that the Commission provides a compliance date for the clearing determination that is shorter than two weeks. The Commission has not provided certainty in this respect. *See Process for Submissions for Review of Security-Based Swaps for Mandatory Clearing and Notice Filing Requirements for Clearing Agencies; Technical Amendments to Rule 19b-4 and Form 19b-4 Applicable to All Self-Regulatory Organizations*, Exchange Act Release No. 34-67286 (June 28, 2012), 77 Fed. Reg. 41602, 41613 (July 13, 2012) (“SEC Clearing Requirement Rule”), available at <https://www.govinfo.gov/content/pkg/FR-2012-07-13/pdf/2012-16233.pdf> (stating that “the timing of implementation of [mandatory clearing] determinations [is] not addressed in the rules being adopted” and that “when a clearing requirement should be implemented will depend on the particular product that the Commission determines is required to be cleared.”).

the proposed 30-day compliance period would still be inadequate given the complex operational and technological steps that must be taken to trade a new SB swap on an SBSEF. Market participants such as regulated funds will need time to onboard to an SBSEF if necessary, and to further update their systems, processes, and procedures to transact via an SBSEF's order book or RFQ system.²⁹

D. The Commission Should Develop a Process to Remove an SB Swap from the Trade Execution Requirement, Including on a Temporary Basis

We also strongly recommend that the Commission modify its proposed approach to removing an SB swap from the trade execution requirement, which would mirror the CFTC's current approach. The proposed approach raises a significant risk that an SB swap may be required to be traded on an SBSEF merely because it is listed on one SBSEF, even if there is no liquidity to sustain trading in that SB swap. Such an outcome could be detrimental for both buy-side and sell-side market participants. To ensure that there is adequate liquidity in SB swaps subject to mandatory execution and provide greater certainty to the SB swap markets, the Commission should adopt a process for removing an SB swap from the MAT scope that is similar to the process for making a MAT determination (as modified by our recommendations above).³⁰

Given the industry's recent experience with the COVID-19 crisis, and consistent with another recommendation in the MRAC Report, we also urge the Commission to consider the implications that a temporary outage at one or more SBSEFs or a major market disruption would have for SB swaps subject to the trade execution requirement. Among other things, the Commission should consider the circumstances under which it would allow for a temporary suspension of the trade execution requirement and any possible terms for such a suspension, as well as any other relief measures the Commission may be able to provide.

E. The Commission Should Consider Creating an Advisory Board to Help Facilitate the MAT Determination Process

We encourage the Commission to create an industry advisory board to provide recommendations both to the Commission and to SBSEFs on SB swaps that should be added or removed from the list of SB swaps that are subject to the trade execution requirements.³¹ The advisory board that

²⁹ We also note that other SBSEFs that do not already list an SB swap that becomes subject to the trade execution requirement, will likely need to update their systems or make other technological changes to be able to offer an order book or RFQ system to allow for trading in that SB swap. Providing adequate implementation time for all SBSEFs would mitigate the risk of a "first mover" advantage to a single SBSEF that is the first to make an SB swap available to trade, a result that would be detrimental to market participant choice.

³⁰ Our recommendations with regards to the removal of an SB swap from the trade execution requirement closely align with the MRAC Report's recommendations. *See* MRAC Report at 3.

³¹ The Commission's 2011 SBSEF Proposal recognized the benefits of creating an advisory body, individual to each SBSEF, with fair representation of market participants, to help determine the SB swaps that should trade on the

the Commission creates should have appropriate expertise and balanced representation, including from the buy side, the sell side, and other stakeholders. This would help further address some of the concerns we have raised regarding the MAT process and ensure that the SB swaps made subject to the trade execution requirement are only the most liquid. Moreover, the advisory board could also help the Commission assess the functioning of the MAT determination process and of the overall SBSEF regulatory framework and provide recommendations for improvement.

IV. We Support the Proposed Exceptions from the Methods of Execution for Required Transactions with Certain Modifications

We strongly support the Commission's alignment of various exceptions from the required methods of execution on SBSEFs under proposed Rule 815 with the CFTC's existing exceptions from the methods of executions on SEFs. The proposed exceptions, which would provide market participants on SBSEFs with necessary trading and operational flexibility, include (i) the time delay requirement for required transactions on an order book; (ii) exceptions for certain package transactions; and (iii) offsetting and correcting trades to resolve error trades. While we also support the proposed exception for block trades, we provide an additional perspective below on the proposed threshold for such trades, including the pre-trade and post-trade implications, and offer several related recommendations.

A. We Recommend a More Tailored Approach to the Proposed Block Trade Exception

We support the Commission's proposed exception for block trades from the required methods of execution on an SBSEF,³² which would provide important flexibility for market participants executing SB swap transactions of a significantly large size. As we have previously explained, rules that facilitate swap block trades allow market participants such as regulated funds to engage in large transactions while mitigating the risks of information leakage and impairment of market liquidity.³³ For purposes of this Proposal, a block trade is defined as an SB swap transaction (not

SBSEF and the SB swaps that should no longer trade on it. *Registration and Regulation of Security-Based Swap Execution Facilities*, Exchange Act Release No. 34-63825 (Feb. 2, 2011), 76 Fed. Reg. 10948, 10968 (Feb. 28, 2011), available at <https://www.govinfo.gov/content/pkg/FR-2011-02-28/pdf/2011-2696.pdf>. While we support the creation of an advisory body that plays a similar role as the one proposed by the Commission in 2011, given the impact of MAT determinations on the entire SB market, we believe that creating a single advisory body for the industry would be more beneficial than having each SBSEF create its own. An industry advisory body would be easier to establish and manage through a centralized process under the Commission's supervision and would be in a better position to make recommendations to all SBSEFs and to the Commission, both on the MAT process as well as on the SBSEF's regulatory framework.

³² Block trades could be executed on the SBSEF's non-order book trading system, or away from the SBSEF's trading system, provided that they are executed pursuant to the SBSEF's rules and procedures. Proposed Rule 802(a).

³³ Letter from Sarah Bessin, Associate General Counsel, ICI, to Christopher Kirkpatrick, Secretary, CFTC (May 22, 2020), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=29311>.

including an equity SB swap) that is subject to public dissemination and, among other things, is “a SB swap based on a single credit instrument (or issuer of credit instruments) or a narrow-based index of credit instruments (or issuers of credit instruments) having a notional size of \$5 million or greater.”³⁴ While we appreciate the Commission’s effort at providing clarity regarding this proposed exception, we recommend that the Commission delay implementation of the required execution methods until it considers its approach to block trades more comprehensively.

Calibrating appropriate block trade threshold sizes for SB swaps has significant implications for market participants from both a pre- and a post-trade transparency perspective. With respect to pre-trade transparency, requiring a fund to disclose its trading interest in an SB swap of a large notional size to multiple participants—via an order book or an RFQ system—would enable opportunistic market participants to piece together information about the fund’s holdings or investment strategy and lead to frontrunning of those potential trades. With respect to post-trade transparency, setting a block trade threshold that is too high would unnecessarily limit the ability to report large-sized SB swap transactions on a delay,³⁵ which would make it difficult for liquidity providers to hedge such positions, leading to higher trading costs and less efficient trading for funds and other market participants.³⁶ The magnitude of these risks depends on, among other factors, an SB swap’s liquidity profile.

We are concerned that applying a single notional threshold—across all applicable SB swaps with respect to SBSEF trading and for any additional future rulemaking related to post-trade public reporting—does not adequately account for varying levels of liquidity across different categories or types of SB swaps. The Commission derived the \$5 million block threshold based on a condition to existing no-action relief that is currently available on a limited basis for credit-based

³⁴ A block trade must also involve an SB swap that is listed on an SBSEF and must be reported subject to the rules and procedures of the SBSEF. Proposed Rule 802(a).

³⁵ In adopting Regulation SBSR in 2015, the Commission did not finalize rules related to block trades, in particular a reporting delay. *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information*, Exchange Act Release No. 34-74244 (Feb. 11, 2015), 80 Fed. Reg. 14564, 14617 (Mar. 19, 2015) (“SBSR Adopting Release”), available at <https://www.govinfo.gov/content/pkg/FR-2015-03-19/pdf/2015-03124.pdf>. Under the current reporting rules, counterparties have up to 24 hours after the time of execution to report most SB swap transactions (including block trades), which would then be publicly disseminated immediately thereafter. *Id.* at 14616. The Commission instead established an “interim phase,” during which period it would collect and analyze data to inform a future rulemaking related to block trades and non-block trades. *Id.*

³⁶ Counterparties to these transactions, which typically are dealers, are willing to provide this liquidity to funds if the dealers can offset the risks of the resulting positions at a reasonable cost. Other market participants’ knowledge of a block trade before the dealer has an adequate time to lay off those risks may provide an opportunity for those seeking to profit from this knowledge to place trades in anticipation of the dealer’s hedging activity, while driving up the price or otherwise attempting to extract a higher premium from the dealer to offset those positions. As a result, those offsetting transactions may become more difficult and costlier to execute, potentially increasing the costs of market making. This risk may cause dealers to raise the costs of providing liquidity for block trades to compensate for the difficulty in hedging their positions in the market. These higher costs, in turn, will be passed on to regulated funds and their investors. To avoid this outcome, funds may be forced to break up block trades into smaller orders, which creates market inefficiencies and may diminish liquidity.

SB swaps³⁷ and further justified this threshold relying merely on single-name CDS transaction data.³⁸ Given the differences in liquidity across different SB swaps, the Commission should instead base its thresholds on more comprehensive transaction data obtained pursuant to Regulation SBSR. Taking such a data-driven approach would allow the Commission to assess the liquidity of different SB swaps based on, for example, swap term, underlying security, and other characteristics.³⁹ This would enable the Commission, similar to the CFTC, to formulate different types or categories of SB swaps and propose differing block trade sizes that are more appropriately tailored to the liquidity characteristics of each type or group.⁴⁰ Importantly, this approach would be consistent with the Dodd-Frank requirement that the Commission, among other things, “[s]pecify the criteria for determining what constitutes a large notional [SB] swap transaction (block trade) *for particular markets and contracts*” (emphasis added).⁴¹

Consistent with our recommendation above, we also recommend that the Commission conduct further analysis before determining block treatment for equity SB swaps. In declining to provide

³⁷ When it imposed that condition, the Commission noted that FINRA applies a \$5 million cap when disseminating transaction reports of economically similar cash debt securities. *See* Proposing Release at 28896.

³⁸ The Commission states that, in proposing block trade thresholds, it “considered the distribution of transaction size in the single-name CDS market, which the Commission believes is representative of the market for [SB swaps] based on a single credit instrument (or issuer of credit instruments) or a narrow-based index of credit instruments (or issuers of credit instruments).” Proposing Release at 28944. We note, however, that the Commission did not apply the criteria that it previously said it would use to determine block trade thresholds, which included: (1) the absolute size of the transaction; (2) the size of the transaction relative to other similar transactions; (3) the size of the transaction relative to some measure of overall volume for that SB swap instrument; and (4) the size of the transaction relative to some measure of overall volume for the security or securities underlying the SB swap. SBSR Adopting Release at 14617.

³⁹ In issuing the Proposal, the Commission considered only a “sample of [SB swap] transaction data that includes certain segments of the market,” including some SB swap transaction data that only started being reported in November 2021 under Regulation SBSR. Proposing Release at 28938-39 (stating that the Commission based its analysis on: DTCC’s data on single-name CDS transactions, which has certain limitations; and on SB swap transaction data reported to SB swap data repositories (SDRs) under Regulation SBSR between November 8, 2021 and February 28, 2022); *SEC Approves Registration of First Security-Based Swap Data Repository; Sets the First Compliance Date for Regulation SBSR*, SEC, Press Release (May 7, 2021), available at <https://www.sec.gov/news/press-release/2021-80> (noting that on November 8, 2021, new rules went into effect requiring SB swap transaction data to be reported to an SDR, and thus made available to the Commission).

⁴⁰ We note that the Commission recently proposed different categories of types of SB swaps—with specified thresholds—for purposes of a large SB swap position reporting framework. *See Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition Against Undue Influence Over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Positions*, Exchange Act Release No. 34-93784 (Dec. 15, 2021), 87 Fed. Reg. 6652 (Feb. 4, 2022), available at <https://www.govinfo.gov/content/pkg/FR-2022-02-04/pdf/2021-27531.pdf>. Further, the Proposal argues that there is no block trade threshold on the CFTC’s side for the Commission to harmonize with, as the CFTC divides swap asset classes into various categories and sets forth a minimum block trade size threshold for each category, but none of those categories corresponds to SB swaps. Proposing Release at 28896.

⁴¹ Exchange Act Section 13m(1)(E).

block treatment, the Proposal merely states, without further analysis or justification, that the Commission's approach follows the CFTC's approach with respect to equity swaps—an approach with which we previously disagreed.⁴² The CFTC reasoned that block treatment of equity swaps for post-trade reporting purposes is not appropriate because (i) a highly liquid underlying cash market for equities exists; (ii) the equity index swaps market is small relative to the futures, options, and cash equity index markets; and (iii) no time delays exist for reporting block trades in the underlying equity cash markets.⁴³ The Commission, however, should undertake additional analysis to demonstrate that these justifications apply equally to the categories or types of equity-based swaps specifically under its jurisdiction, which include, for example, total return swaps based on a single security or loan, or a narrow-based security index.⁴⁴

We further recommend that, as part of its analysis, the Commission determine whether block treatment would be appropriate for equity-based SB swaps in the pre-trade transparency context. Similar to other categories or types of large-sized SB swaps that would qualify for block treatment, flexible execution with respect to large-sized, equity-based SB swaps is important to avoid information leakage regarding a market participant's investment strategies.⁴⁵

V. The Commission Should Address the Use of Pre-Execution Communications

We request that the Commission address the extent to which market participants may utilize “pre-execution communications”⁴⁶ when trading on an SBSEF. The CFTC has specified that

⁴² Letter from Karrie McMillan, General Counsel, ICI, to David Stawick, Secretary, CFTC, at 5 (May 14, 2012), available at <https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=24378>.

⁴³ *Procedures To Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades*, 78 Fed.Reg. 32866, 32884 (May 31, 2013) <https://www.govinfo.gov/content/pkg/FR-2013-05-31/pdf/2013-12133.pdf>. The CFTC maintained this reasoning in recent changes to its real-time reporting rules but stated that it “will continue to assess the equity asset class when it recalculates the block levels every year.” *Real-Time Public Reporting Requirements*, 85 Fed. Reg. 75422, 75448-49 (Nov. 25, 2020), available at <https://www.govinfo.gov/content/pkg/FR-2020-11-25/pdf/2020-21568.pdf>.

⁴⁴ *Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”*; *Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, Exchange Act Release Nos. 33–9338; 34–67453 (July 18, 2012), 77 Fed. Reg. 48208, 48264 (Aug. 13, 2012), available at <https://www.govinfo.gov/content/pkg/FR-2012-08-13/pdf/2012-18003.pdf>.

⁴⁵ We note that with respect to underlying cash equities, the Commission does define what constitutes a block trade. See, e.g., Rule 600(a)(9) of Regulation NMS, which defines “block size” as an order that is: (i) at least 10,000 shares or (ii) a quantity of stock having a market value of at least \$200,000.

⁴⁶ For instance, the CFTC defines “pre-execution communications” as “communications between market participants to discern interest in the execution of a transaction prior to the exposure of the market participant's orders (e.g., price, size, and other terms) to the market; such communications include discussion of the size, side of market, or price of an order, or a potentially forthcoming order.” *Swap Execution Facilities and Trade Execution*

such communications may occur pursuant to a SEF's rules that have been certified to or approved by the [CFTC].⁴⁷ Unlike the CFTC, however, the Commission does not set forth parameters or guidance with respect to what constitutes pre-execution communications when trading on SBSEFs. The Commission should align its rules with those of the CFTC in this respect, given that pre-execution communication is a standard market practice that investment advisers use to guard against information leakage and obtain fair pricing for large-sized trades and package transactions, among other types of transactions, on behalf of funds and other clients.

VI. The Commission Should Align Its Cross-Border Application with the CFTC's Approach

With respect to the cross-border application of trading venue and trade execution requirements for SB swaps, we urge the Commission to ensure that its proposed approach to granting exemptions will produce outcomes similar to those of the CFTC. The CFTC has granted exemptions from SEF registration to foreign swap trading facilities in the European Union, Japan, and Singapore and has determined that such facilities can be used to execute swaps that are subject to the CFTC's trade execution requirement.⁴⁸ The CFTC provided these exemptions (1) based on requests from regulators on behalf of the facilities under each of their respective jurisdiction; and (2) after finding that these facilities are "subject to comparable, comprehensive supervision and regulation" by their respective regulators.

To further harmonize with the CFTC's SEF framework, and promote consistency and simplicity, we recommend that the Commission apply its standards under proposed Rule 833 in a manner that would align the scope of its exempted venues with those venues that have obtained an exemption from the CFTC. We are concerned about potential misalignment, given that the Commission notes that it would not necessarily be required to utilize the CFTC's standard for equivalence and could provide an exemption if doing so is "necessary or appropriate in the public interest, and consistent with the protection of investors."⁴⁹ US-based investment managers, some of which manage non-US regulated funds, would likely seek to utilize the same trading venues for trading SB swaps as they use today for trading swaps, both in and outside the US. These investment managers would face significant costs and burdens if the two regulatory approaches produce different outcomes for swaps and SB swaps regarding where a transaction may be executed. Further, these managers could face an unintended economic disadvantage if other global market participants avoid trading with the managers' non-US fund clients solely to avoid being subject to the Commission's SBSEF requirements.

Requirement, 83 Fed.Reg 61946, 61985 (Nov. 30, 2018) ("CFTC 2018 Proposal"), available at <https://www.govinfo.gov/content/pkg/FR-2018-11-30/pdf/2018-24642.pdf>.

⁴⁷ 17 CFR 37.203(a).

⁴⁸ CFTC, Exemption of Foreign Swap Trading Facilities from SEF Registration, <https://www.cftc.gov/International/ForeignMarketsandProducts/ExemptSEFs>.

⁴⁹ See Proposing Release at 28924 n. 246.

Ms. Vanessa Countryman
June 10, 2022
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We hope that this information and our recommendations are helpful to the Commission in developing an effective regulatory framework for SBSEFs. If you have any questions, please contact Sarah Bessin at [REDACTED] or Nicolas Valderrama at [REDACTED]

Regards,

/s/ Sarah A. Bessin

/s/ Nicolas Valderrama

Sarah A. Bessin
Associate General Counsel

Nicolas Valderrama
Counsel

cc: The Honorable Gary Gensler
The Honorable Alison H. Lee
The Honorable Hester M. Peirce
The Honorable Caroline A. Crenshaw

Haoxiang Zhu, Director
Michael Gaw, Assistant Director
Division of Trading and Markets

Securities and Exchange Commission