



January 18, 2011

Elizabeth Murphy, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549–1090

Re: Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information
(File Number S7–34–10)

Dear Ms. Murphy:

The Wholesale Market Brokers' Association, Americas (“WMBAA” or “Association”)¹ appreciates the opportunity to provide comments to the Securities and Exchange Commission (“SEC” or “Commission”) on the proposed Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information (“Regulation SBSR”) under the Securities Exchange Act of 1934 (“Exchange Act”).²

Summary of Response

As the Commission contemplates an appropriate regulatory regime for reporting and dissemination of security-based swap (“SBS”) information, the WMBAA believes it is incumbent upon the Commission to follow the direction given in section 13(m)(1)(E) of the Exchange Act, which requires that the Commission’s rule providing for the public availability of SBS transaction and pricing data contain provisions that take into account whether public disclosure will materially reduce market liquidity. The WMBAA, as an association representing the largest inter-dealer brokers in OTC markets, believes that the impact of these rules on market liquidity is highly dependent on how the policy governing large block trading is finalized. If the policy governing block trades does not properly define such a trade, the WMBAA remains very concerned that possible rules related to the calculation of a block trade threshold and trade reporting could negatively impact market liquidity, disturbing businesses’ ability to hedge commercial risk, to appropriately plan for the future and, ultimately, stifle economic growth and job creation.

The WMBAA is pleased to offer its comments related to: (i) appropriate methods to calculate block trade thresholds; (ii) appropriate entities to calculate and publish block trade thresholds; (iii) post-trade dissemination of block trades; and (iv) the publication of market data by market participants.

¹ The WMBAA is an independent industry body representing the largest inter-dealer brokers (“IDBs”) operating in the North American wholesale markets across a broad range of financial products. The WMBAA and its member firms have developed a set of *Principles for Enhancing the Safety and Soundness of the Wholesale, Over-The-Counter Markets*. Using these *Principles* as a guide, the WMBAA seeks to work with Congress, regulators, and key public policymakers on future regulation and oversight of over-the-counter (“OTC”) markets and their participants. By working with regulators to make OTC markets more efficient, robust and transparent, the WMBAA sees a major opportunity to assist in the monitoring and consequent reduction of systemic risk in the country’s capital markets.

² See Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information, 75 Fed. Reg. 75,208 (December 2, 2010).

Discussion of Proposed Regulation SBSR

As interdealer brokers involved in the formulation and execution of large derivatives transactions between swap and security-based swap dealers, the distinction between block and non-block trades is vital to ensure OTC derivatives markets can continue to provide liquidity to and be a source for risk mitigation for end-users.

It is important that the Commission recognize that OTC derivatives markets are different than financial markets that have significant retail participation.³ While the relationship between exchange-traded and OTC markets generally has been complimentary, as each market typically provides unique services to different trading constituencies for products with distinctive characteristics and liquidity needs, the nature of trading liquidity in the exchange-traded and OTC markets is fairly different. Liquidity is the degree to which a financial instrument is easy to buy or sell quickly with minimal price disturbance. The liquidity of a market for a particular financial product or instrument depends on several factors, including: the number of market participants and facilitators of liquidity, the degree of standardization of instrument terms, and the volume of trading activity.

Highly liquid markets exist for both commoditized, exchange-traded products, and more standardized OTC instruments, such as the market for U.S. treasury securities, equities and certain commodity derivatives. Exchange-traded markets provide a trading venue for fairly simple and commoditized instruments that are based on standard characteristics and single key measures or parameters. Exchange-traded markets rely on relatively active order submission by buyers and sellers and generally high transaction flow. These markets allow a broad base of trading customers meeting relatively modest margin requirements to transact standardized contracts in a relatively liquid market. As a result of the high number of market participants and the relatively small number of standardized instruments traded, liquidity in exchange-traded markets is relatively continuous in character.

In comparison, many swaps markets feature a broader array of less-commoditized products and larger-sized orders that are traded by fewer counterparties. Trading in these markets is characterized by variable or non-continuous liquidity. Such liquidity can be said to be episodic, with liquidity peaks and troughs that are seasonal (certain energy products) or more volatile and tied to external market conditions (certain credit products).

As a result of the episodic nature of liquidity in certain swaps markets with fewer participants, we believe that the CFTC and SEC need to carefully structure a clearing and reporting regime for block trades that is not a “one size fits all” approach, but rather takes into account the unique challenges of fostering liquidity in the broad range of swaps markets, provides for the transacting of larger transactions without unnecessary regulatory burdens, and does not materially reduce market liquidity.

³ See, e.g., Comments from Yuhno Song, Merrill Lynch, (“I think one of the distinctions we have is a market that may be more smaller in retail based versus a market that is with far small number of participant and that’s institutional based.”) Public Roundtable to Discuss Swap Data, Swap Data Repositories, and Real Time Reporting, September 14, 2010 (“Roundtable Transcript”) at 332-333. Available at: <http://www.cftc.gov/ucm/groups/public/@swaps/documents/file/derivative18sub091410.pdf>.

Formulation of Block Trade Threshold

While the WMBAA believes that each asset class and each swaps instrument has a threshold amount that could be calculated and used to distinguish between typical and block trades, its primary concern is that the block trade exceptions be individually set for the unique liquidity requirements of the broad range of swaps instruments so that the process of completing a block trade is appropriately defined and trading may continue without adversely impacting market participants' ability to place, exit or hedge their trades.

With respect to block trade thresholds, while the appropriate threshold amount will differ by asset class and instrument, the notion of a block trade involves more than merely the size of a transaction. The WMBAA member firms have witnessed an evolution in interdealer markets with the development of a process referred to as "work-up." In this model, once a price is agreed for trading, the resultant trade is reported to market participants and they are offered the opportunity to join the trade and increase liquidity. Work-up enables traders to assess the markets in real-time and make real-time decisions on trading activity, without the fear of moving the market one way or another. It is vital that any block trade calculation recognize the role work-up plays in forming liquidity. This is done to allow the market to find the appropriate pricing levels to optimally complete the transaction without prematurely causing the market impact of a large block.

The WMBAA believes it is appropriate to provide regulators with necessary market information for oversight purposes, but the public dissemination of incremental activity that would otherwise constitute a block trade could jeopardize identification of counterparties and materially reduce market liquidity, which does not comport with the reporting goals enumerated in the Dodd-Frank Wall Street Reform and Consumer Protection Act.⁴

Congress recognized the importance of tailored block trade thresholds specific to an asset class and instrument.⁵ The WMBAA advocates, as an example, a tiered solution for SBS classification and reporting. The first tier would include all "social" size trades, which must be reported immediately to market participants. The second tier would include trades that are a certain multiple of the "social" size, dependent on the maturity, underlying credit, and frequency of recent transactions in the specific instrument. Each of these transactions would be reported to a security-based swap data repository ("SDR") within 15 minutes of trade execution. This, the WMBAA believes, would be acceptable to the market participants in as much as it would be less disruptive to their ability to place, hedge or exit positions. Finally, the WMBAA would suggest a third tier for trades greater than twice the amount of the block trade threshold, reported with an indication that an extremely large block trade was executed.

⁴ Pub. L. No. 111-203, H.R. 4173.

⁵ Statement of Senator Blanche Lincoln ("The committee expects the regulators to distinguish between different types of swaps based on the commodity involved, size of the market, term of the contract and liquidity in that contract and related contracts, i.e; for instance the size/dollar amount of what constitutes a block trade in 10-year interest rate swap, 2- year dollar/euro swap, 5-year CDS, 3-year gold swap, or a 1-year unleaded gasoline swap are all going to be different."). Senate Congressional Record S. 5921, July 15, 2010.

Such a reporting regime would ensure market participants retain a level of transparency acceptable to successful trading. It is important to distinguish between public reporting to market participants and regulatory reporting through the SDR, which would be privy to complete trade information. By identifying an appropriate social size, the Commission would encourage additional market participants to post prices and provide liquidity on electronic platforms. This, in turn, would support the Commission's objective of increasing the number of market makers and bringing greater transparency into the swaps markets.

Block Trade Calculation and Publication

Proposed Regulation SBSR contemplates that a registered SDR would be responsible for establishing and maintaining written policies and procedures for calculating and publicizing block trade thresholds for all security-based swap instruments reported to the registered SDR in accordance with the criteria and formula for determining block size as specified by the Commission.⁶ Under this framework, the Commission would specify the criteria and formula for determining block size based on the limited information provided to it consisting of SBS transaction data reported to an SDR for completed SBSs. Such information only provides a partial picture of the liquidity challenges of a particular SBS marketplace. There is other information, such as the size and quantity of bids and offers that do not result in completed transactions, that is available to security-based swap execution facilities ("SB SEFs") as neutral intermediaries in the market.

The WMBAA believes that it is necessary to consider this more complete scope of information in calculating block trade thresholds that are truly appropriate for security-based swap markets. The WMBAA therefore proposes the formation of a block trade standards setting board (the "Security-Based Swaps Standards Board") made up of recognized experts and representatives of registered SDRs and SB SEFs to make recommendations to the Commission for appropriate block trade thresholds for SBSs.

The Security-Based Swaps Standards Board would work with the Commission to establish and maintain written policies and procedures for calculating and publicizing block trade thresholds for all SBSs reported to the registered SDR in accordance with the criteria and formula for determining block size as specified by the Commission. The Security-Based Swaps Standards Board would also undertake market studies and research at its expense as is necessary to establish such standards. This arrangement would permit SB SEFs, as the entities most closely related to block trade execution, to provide essential input into the Commission's block trade determinations and work with registered SDRs to distribute the resulting threshold levels to SB SEFs. Further, the proposed regulatory structure would reduce the burden on SDRs, remove the possibility of miscommunication between SDRs and SB SEFs, and ensure that SB SEFs do not rely upon dated or incorrect block trade thresholds in their trade execution activities.

Further, if there is more than one registered SDR for an asset class, it may prove difficult for the Commission to ensure that all registered SDRs calculate the same block trade thresholds for the same SBS instruments. In comparison, one common regulatory organization responsible for facilitating SB SEF compliance with core principles will be uniquely situated to prevent the problem

⁶ See 75 Fed. Reg. at 75,287.

posed by multiple SDRs, which becomes further exacerbated if there are multiple registered SDRs in the same asset class each with individual market data feeds that need to be aggregated to calculate block trade thresholds.

The determination whether an SBS transaction is a block trade should reflect a risk-weighted basis, calculated on an instrument-by-instrument basis. This threshold should be updated at an appropriate time interval, taking into account the unique liquidity characteristics and challenges of the market in which the instrument trades. Any formulaic approach to computing the thresholds from trade size or other population parameters should reflect the number of participants in the market, the frequency of trading activity (daily, weekly and monthly) and the average trade sizes and terms of the transactions.

The established block trade threshold could be subject to gaming, particularly if the market perceives the threshold to be arbitrarily determined. However, if the block threshold accurately captures the risk and liquidity parameters related to trading activity, then gaming would be ineffective, and less likely to occur.

With respect to inter-affiliate transactions or trades resulting from portfolio compression, the WMBAA believes that if the block thresholds are appropriately calculated, market participation will increase, resulting in additional transparency and markets that better serve the public interest. If the block trade levels allow market makers time to appropriately hedge the risk that they've committed capital to, then they will be better able to continue to provide liquidity.

Reporting of Block Trades

The Commission remarks in the preamble to proposed Regulation SBSR that because the registered SDR, and not the reporting party, would have the responsibility to determine whether a transaction qualifies as a block trade, the reporting party would be required to report an SBS to a registered SDR or the Commission pursuant to the time frames set forth in Rules 901(c) and (d), regardless of whether the reporting party believes the transaction qualifies for block trade treatment. Proposed Regulation SBSR does not include a delay in reporting block trades to a registered SDR.⁷

As noted in a previous letter, the WMBAA is supportive of trade reporting for all trades as soon as technologically practicable. The Association believes that all trade reporting, regardless of size, should be reported to the SDR. The WMBAA members each possess the technological capabilities to provide regulators with real-time electronic trade information for transactions executed in multiple financial markets.⁸

⁷ See *id.* at 75,233.

⁸ See, e.g., Comments from Shawn Bernardo, Tullett Prebon Americas Corp., representing Wholesale Markets Brokers Association, ("All of the brokers have the capability to report trades to the regulators in a timely fashion . . . as far as TRACE is concerned, we have a track record of reporting those trades efficiently, and we have the systems in place to do that, along with the various means . . . we can do that voice, we can do it electronically, we can do it as hybrid as far as the execution, but we send those trades electronically to them in a timely fashion.") Roundtable Transcript at 227-228.

While the WMBAA believes that posting the full details of SB SEF-executed transactions to market participants should be at the core of the SB SEF obligations, the reporting obligations of the SB SEF should reflect the information that the SB SEF possessed at the time of the transaction. The SB SEF should not have the primary reporting obligations. The SB SEF would likely not be privy to all of the terms required to be reported in accordance with proposed Regulation SBSR, such as, but not limited to: (i) contingencies of the payment streams of each counterparty to the other; (ii) the title of any master agreement or other agreement governing the transaction; (iii) data elements necessary to calculate the market value of the transaction; and (iv) other details not typically provided to the SB SEF by the customer, such as the actual desk on whose behalf the transaction is entered. Moreover, and quite critical, an SB SEF would not be in a position or necessarily have the capabilities to report life cycle event information. Indeed, even if an SB SEF were required to report the transaction details as the proposed regulation requires, something we do not think advisable, it would likely take at least 30 minutes to gather and confirm the accuracy of that information.

Additionally, the post trade reporting requirements may have an adverse effect on liquidity, particularly with respect to larger transactions since the reporting of larger transactions will likely have the effect of causing participants to refrain from entering the market which those participants might not otherwise have done, adversely impacting the ability of the parties to the large transaction to mitigate the risks of that transaction by entering into separate, offsetting transactions. This could effect a party's ability to hedge its risks and mitigate the exposure of that legitimate hedge will be diminished, resulting in fewer transactions of that nature and potentially widening spreads, which in turn will increase end-user costs.

Nevertheless, the WMBAA believes that trading counterparties with reporting obligations should be able to contract with a SB SEF to handle the reporting process without transferring their reporting obligations. This will put smaller counterparties with limited trading reporting technology in a less disadvantaged trading position to larger trading counterparties.

Dissemination of Block Trade Information

Under proposed Regulation SBSR, a registered SDR must publicly disseminate a transaction report of an SBS that constitutes a block trade immediately upon receipt of information about the block trade from the reporting party. Under proposed Regulation SBSR, the market participants will learn the price, but not the size, of an SBS block trade in real-time. The transaction report must contain all of the information required under the real-time reporting rules, including the transaction ID and an indicator that the report represents a block trade. The SDR is required to publicly disseminate a complete transaction report for a block trade (including the transaction ID and the full notional size) as follows:

- If the SBS was executed on or after 05:00 Coordinated Universal Time ("UTC") and before 23:00 UTC of the same day (which corresponds to 12:00 midnight and 6:00 p.m. EST), the transaction report (including the transaction ID and the full notional size) will be disseminated at 07:00 UTC of the following day (which corresponds to 2:00 a.m. EST of the following day).
- If the SBS was executed on or after 23:00 UTC and up to 05:00 UTC of the following day (which corresponds to 6:00 p.m. until midnight EST), the transaction report (including the transaction ID and the full notional size) will be disseminated at 13:00 UTC of that following day (which corresponds to 8:00 a.m. EST of the following day).

All block trades will have at least an eight-hour delay before the full notional size will be disseminated. The established cut-off time will be 23:00 UTC, which corresponds to 6:00 p.m. EST. Block trades executed on or after 05:00 UTC (which corresponds to midnight EST) and up to 23:00 UTC (6:00 p.m. EST) will have to have their full notional size disseminated by 07:00 UTC, which corresponds to 2:00 a.m. EST. Under the proposed approach, block trades executed during a period that runs roughly from the close of the U.S. business day to midnight EST will have their full sizes disseminated by a registered SDR at a time that corresponds to the opening of business on the next U.S. day. If a registered SDR is in normal closing hours or special closing hours at a time when it will be required to disseminate information about a block trade pursuant to this section, the registered SDR must disseminate that information immediately upon re-opening.

The WMBAA would suggest that disseminating the specific notional amount of a block could jeopardize the anonymity of the counterparties to such trades, making counterparties less willing to engage in transactions of size. Further, the effect of having no delay, or only a short dissemination delay, for a block trade report that includes the full notional size will discourage market makers from committing capital and providing liquidity to the broader market. From a market perspective, there is little gain from disseminating full notional size information. Consistent with the experiences from the implementation of the Financial Industry Regulatory Authority's Transaction Reporting and Compliance Engine ("TRACE"), which provides regulators with full trade information and publicly disseminates trades within a size range, the WMBAA believes the Commission should implement a public reporting methodology. This benefits market participants without exposing a trade's notional size, which protects counterparty anonymity, and preserves liquidity and price competition in the market.⁹

Additionally, market participants will be wary of committing to larger sized transactions knowing the rapidity in which other participants will gain knowledge of these trades, leading to less liquidity for the dealer market, and ultimately for end-user participants. The WMBAA also believes that the public dissemination of block trades, as proposed, will allow some market participants to infer the identity of the parties to the transaction and materially reduce market liquidity.

If a liquidity provider perceives greater danger in supplying liquidity, it will step away from providing tight spreads and leave those reliant on market maker liquidity with poorer hedging opportunities. From a market structure standpoint, liquidity "takers" benefit from liquidity providers acting in a competitive environment. The liquidity providers compete with each other, often deriving very small profits per trade from a large volume of transactions. By relying on their ability to warehouse trades and post capital to make markets and using their distribution and professional know-how to offer competitive prices to their customer base, market makers provide liquidity essential to fulfill the need of hedgers. For these reasons, having either no delay or a short dissemination delay will actually erode price discovery and the level of price efficiency in the market.

⁹ See 75 Fed. Reg. at 75,232, fn. 108. ("If the par value of the trade exceeds \$5 million (in the case of investment grade bonds) or \$1 million (in the case of non-investment-grade bonds) the quantity disseminated by TRACE will be either "5 million+" or "1 million+". At no time will TRACE subsequently disseminate the full size of the trade. See TRACE User Guide, version 2.4 (last update March 31, 2010), at 50.")

Publication of Market Data

Proposed Regulation SBSR contemplates that no person other than a registered SDR can make available to one or more persons (other than a counterparty) transaction information relating to an SBS before the earlier of 15 minutes after the time of execution of the security-based swap, or the time that a registered SDR publicly disseminates a report of that security-based swap.¹⁰ The preamble indicates that other private sources of market data reflecting subsets of the security-based swaps market could arise. The Commission remarks in the preamble to proposed Regulation SBSR that SB SEFs would have information about SBSs executed on its systems and could find that commercial opportunities exist to sell such information.¹¹ In a related release, the Commission's proposed regulation concerning Security-Based Swap Data Repository Registration, Duties, and Core Principles does not specifically address commercial use of SBS data.¹² However, under proposed 17 C.F.R. § 240.13n-4(c)(3)(iii) the third core principle – rules and procedures for minimizing and resolving conflicts of interest – requires an SDR to establish, maintain and enforce policies and procedures regarding the SDR's non-commercial and/or commercial use of SBS data.¹³ In connection with the preamble discussion of this requirement, the SEC makes several requests for comment on an SDR's commercial use of data.¹⁴

The WMBAA member firms will report the required SBS transaction information to a registered SDR in the mandated time frame as set forth in Commission regulations. However, the provisions of such information to SDRs should be for the specific and limited purpose of the SDR fulfilling specific regulatory requirements (reporting data to regulators for regulatory oversight and enforcement, public reporting of trade information as specifically prescribed by the Commission). Reporting such data to an SDR by a reporting entity (*e.g.* an SB SEF or any other party reporting the transaction information) should not relinquish ownership of such data by the SB SEF or other reporting entity and would also not inhibit its right to use the data for other purposes. Consistent with reporting practices in other markets, the reporting of SBS transaction information to a registered SDR should not bestow the SDR with the authority to use the SBS transaction data for any purpose other than those explicitly enumerated in the Commission's regulations.

The WMBAA is concerned that proposed rules inhibit an SB SEF's ability to continue to have ownership and control over its data and the ability to sell that data to the marketplace. The WMBAA would suggest that Section 242.902(d) of proposed Regulation SBSR be revised in such a way that an SDR would accept and maintain SBS transaction data for use by regulators, but the SBS counterparties and SB SEFs continue to have the ability to market and commercialize their own proprietary data. This could be achieved, in part, by requiring SDRs to include such a provision in its required policies and procedures regarding the SDR's non-commercial and/or commercial use of SBS data required to be established, maintained and enforced by the Commission's proposed SDR

¹⁰ See 75 Fed. Reg. at 75,286.

¹¹ See *id.* at 75,242, fn. 153.

¹² See Security-Based Swap Data Repository Registration, Duties, and Core Principles, 75 Fed. Reg. 77,306 (December 10, 2010).

¹³ See *id.* at 77,369.

¹⁴ See *id.* at 77,325-26.

rules. Ultimately, the WMBAA urges the Commission to take caution in implementing a regulation that could be inconsistent with existing models in equity and futures markets and might prevent entities with the necessary technological capabilities from capturing, publishing, and monetizing data for purposes outside of regulatory oversight.

Conclusion

The WMBAA thanks the Commission for the opportunity to comment on the proposed Regulation SBSR. Please feel free to contact the undersigned with any questions you may have on our comments.

Sincerely,

A handwritten signature in black ink, appearing to read 'Julian Harding', with a long horizontal flourish extending to the right.

Julian Harding, Chairman