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February 13, 2012

Mr. David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: **RIN 3038-AD18 – Process for a Designated Contract Market or Swap Execution Facility To Make a Swap Available To Trade**

Dear Mr. Stawick:

The Commodity Futures Trading Commission ("CFTC") has requested public comment on proposed rules to establish a process for a swap execution facility ("SEF") or a designated contract market ("DCM") to make a swap "available to trade" under Section 2(h)(8) of the Commodity Exchange Act ("CEA"), as amended by Dodd-Frank. *See* 76. Fed. Reg. 77728 (Dec. 14, 2011) (the "Proposed Rules"). The CFTC is to be commended for its diligent efforts to formulate appropriate and workable rules that will promote swap trading on organized, regulated platforms—a key reform objective endorsed by Congress. *See* Dodd-Frank §733, adding CEA § 5h(e). Unfortunately, the CFTC's proposal could unintentionally thwart achieving that objective.

MarketAxess Corporation ("MarketAxess") operates a leading electronic trading platform for investment industry professionals that promotes transparency, price discovery, and liquidity in the corporate bond and other markets, including credit default swaps ("CDS").[1] MarketAxess' current operations are consistent with the CFTC's SEF proposals for trading protocols, price transparency, audit trails, independence,[2] and financial resources. As soon as the CFTC finalizes its SEF rules and registration process, MarketAxess intends to apply for registration as a SEF and to offer a transparent, electronic Request for Quote System for those CDS products that are subject to the CFTC's jurisdiction.

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[1] MarketAxess Corporation is the principal operating subsidiary of MarketAxess Holdings Inc., a public company. We are regulated as a broker-dealer and as an alternative trading system operator by the U.S. Securities and Exchange Commission and the Financial Industry Regulatory Authority. Our principal offices are located in New York City, and we currently employ approximately 232 persons.

[2] Although initially a dealer-owned entity, MarketAxess Holdings Inc. is now a public company, with no dealer(s) owning, individually or in the aggregate, more than 20% of MarketAxess' common stock. In addition, MarketAxess' nine-person Board of Directors includes seven individuals who meet the requirements for independence under the rules of the Nasdaq Stock Market.

We therefore have an acute interest in, and appreciate the opportunity to submit public comment on, the CFTC's proposals that affect SEFs.

I. Congress Did Not Authorize the CFTC to Create a Process to Determine Which Swaps Are "Available to Trade."

A. The Statute Contemplates no "Made Available to Trade" SEF or CFTC Determination.

As amended by Dodd-Frank, the CEA provides that some swaps will be subject to a clearing mandate and some (or all) of these swaps will be subject to a trade execution mandate (and thus must be traded and executed on a SEF or DCM). *See* Dodd-Frank §723(a), adding CEA § 2(h). In the statute, Congress omitted any mention of the CFTC (or anyone else) making a formal determination whether a swap must be traded and executed on a regulated platform. Congress similarly omitted any mention in the statute of any process whatsoever for determining which swaps will be subject to the trade execution mandate. Instead, Congress simply stated: **all** swaps that are subject to the clearing mandate must be traded on a SEF or a DCM[3] **unless** that swap is not made **"available to trade"** on **any** SEF or DCM or one party to the swap is a commercial end user that is exempt from the clearing and trade execution requirements.[4]

In other words, the statute provides that non-exempt market participants will be required to trade and execute a swap on a SEF *if and only if* the following two conditions are met: (i) the CFTC has decided that the swap is subject to the clearing mandate; and (ii) trading the swap on a SEF is possible because the swap is available to be traded on a SEF. On its face, the statute thus considers whether a swap is "available to trade" on a regulated market to be a purely factual inquiry. It either is or it is not. Congress did not contemplate, or authorize the Commission to add, a third condition that the CFTC, SEF or anyone else determine that the swap is required to be traded and executed on a regulated platform.[5]

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[3] For simplicity, we will refer to SEFs in the balance of the letter, but intend for our SEF references to refer to DCMs as well.

[4] Dodd-Frank § 723(a), adding Commodity Exchange Act § 2(h)(8) reads as follows:

"(A) IN GENERAL.—With respect to transactions involving swaps subject to the clearing requirement of paragraph (1), counterparties shall—

"(i) execute the transaction on a board of trade designated as a contract market under section 5; or
"(ii) execute the transaction on a swap execution facility registered under 5h or a swap execution facility that is exempt from registration under section 5h(f) of this Act.

"(B) EXCEPTION.—The requirements of clauses (i) and (ii) of subparagraph (A) shall not apply if no board of trade or swap execution facility makes the swap available to trade or for swap transactions subject to the clearing exception under paragraph (7)." [The reference to § 5h(f) is intended to reference § 5h(g).]

[5] The language of the statute is clear and unambiguous in contrast to statements in the legislative history, which depart from the terms of the statute and surely provide no basis for the time-consuming, costly, and redundant process that the Proposed Rules would impose. *See* Statement of Senator Blanche Lincoln, Congressional Record (July 15, 2010) S5921 (stating that "swaps ... determined to be subject to the mandatory clearing requirement by the [CFTC] would also be required to be traded on a [DCM] ... or [SEF] .... To avoid any

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B. When Congress Intended the CFTC to Have a Formal Determination Process, Congress Included the Process Explicitly in the Text of the Statute.

In the same section of Dodd-Frank (§723(a), adding CEA § 2(h)) as the trading mandate, Congress directs the CFTC to adopt a formal process to implement the clearing mandate (which the CFTC has done). The statute requires the CFTC to make a determination, following a specified procedure, whether a swap will become subject to the clearing mandate based on the following five factors:

1. The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data;

2. The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded;

3. The effect on the mitigation of systemic risk, taking into account the size of the market for the contract and the resources of the derivatives clearing organization available to clear the contract;

4. The effect on competition, including appropriate fees and charges applied to clearing; and

5. The existence of reasonable legal certainty in the event of the insolvency of the relevant derivatives clearing organization or one or more of its clearing members with regard to the treatment of customer and swap counterparty positions, funds, and property. *See* Dodd-Frank § 723(a), adding CEA § 2(h)(2)(D); *See also* Process for Review of Swaps for Mandatory Clearing, 76 Fed. Reg. 44464 (July 26, 2011).

As evidenced by the presence of the specific determination process in Dodd-Frank's clearing mandate, when Congress intended the CFTC to follow a formal determination process, Congress included the process explicitly in the statute. As discussed above, Congress failed to even mention any determination or formal process in Dodd-Frank's trade execution mandate; this omission reflects the simple fact that Congress did not intend, or even envision, a separate formal "made available to trade" process.

Unlike the clearing mandate, the trade execution mandate was to be self-executing. If a swap was subject to the clearing mandate and non-exempt market participants could trade that swap on a SEF, then the trade execution mandate applied. Moreover, in the context of the

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conflict of interests, the [CFTC] will make a determination as to what swaps must be cleared following certain statutory factors."). *But see id.* at S5923 (stating that "in determining whether a [SEF] 'makes the swap available to trade,' the CFTC should evaluate not just whether the [SEF] permits the swap to be traded on the facility, or identifies the swap as a candidate for trading on the facility, but also whether, as a practical matter, it is in fact possible to trade the swap on the facility.").

clearing mandate, the CFTC would have already considered whether a swap has significant outstanding notional exposures, trading liquidity, and adequate pricing data. Therefore, as recognized by Congress, there is no need for the CFTC to receive and review additional submissions on the tradability of that swap.

C. More Swaps Would Be Subject to the Trade Execution Mandate, Furthering a Key Goal of Dodd-Frank, If No Formal Determination Process is Imposed.

i. Under the Proposed Rules, Not All Swaps Subject to the Clearing Mandate and Available to Trade on a SEF Would be Subject to the Trade Execution Mandate.

The Proposed Rules would elevate the "made available to trade" exception to the trade execution mandate to a formal regulatory finding that needs to be made before a swap could be required to be traded and executed on a regulated platform. As proposed, a swap would not become subject to the trade execution mandate until:

1. A SEF reviews the swap, taking into account any factor the SEF may consider to be relevant, including, but not limited to, any one or more of seven enumerated factors; [6]

2. The SEF determines that it makes the swap available to trade and documents its analysis;

3. The SEF submits its determination and analysis to the CFTC and either requests that the CFTC approve its submission pursuant to CFTC Rule 40.5 or self-certifies that its submission complies with the rules pursuant to CFTC Rule 40.6; and

4. The CFTC reviews and approves a submission filed for approval (45 or 90 day process) or reviews and does not disturb a self-certified submission (10 or 100 day process).[7]

No swap would be required to be traded and executed on a regulated platform unless a SEF and the CFTC completed all the proposed steps. That means, even if a swap is traded on a

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[6] The seven factors listed in the Proposed Rules are:

i. Whether there are ready and willing buyers and sellers;
ii. The frequency or size of transaction on SEFs, DCMs, or bilateral transactions;
iii. The trading volume on SEFs, DCMs, or of bilateral transactions;
iv. The number and types of market participants;
v. The bid/ask spread;
vi. The usual number of resting firm or indicative bids and offers; and
vii. Whether a SEF's trading system or platform or a DCM's trading facility will support trading in the swap.

[7] Our understanding from the Commission staff roundtable held on January 30 is that the Commission would initially treat each submission as presenting novel or complex issues that require additional time to analyze. As a result, no "made available to trade" determination submitted by a SEF could take effect until 90 days after the SEF files the submission for approval or 100 days after the SEF files a self-certified submission.

SEF and the CFTC finds in the context of its clearing mandate determination that trading in the swap is liquid, the four steps in the Proposed Rule must be followed.

ii. The Proposed Rules Preclude Exempt SEFs from Making Swaps Available to Trade.

The Proposed Rules could also reduce the number of swaps that become subject to the trade execution mandate because of issues that arise for SEFs that are exempt from CFTC registration. Under CEA § 5h(g), a SEF may be exempt from registering with the CFTC if the CFTC finds that the SEF is subject to comparable regulation by the Securities and Exchange Commission, a prudential regulator, or the SEF's home country. CEA § 2(h)(8) provides that a swap that is required to be cleared must be traded and executed on: a DCM; a registered SEF; or an exempt SEF *if* **any** SEF (whether registered or exempt) makes the swap available to trade.[8] The statute thus contemplates that an exempt SEF could make swaps available to trade for purposes of the trading mandate. An exempt SEF is not a registered entity, however, and only registered entities are eligible to submit determinations for voluntary approval or through self-certification under CFTC Rules 40.5 and 40.6.

Therefore an exempt SEF would seem to be precluded from submitting a "made available to trade" determination for voluntary CFTC approval or via self-certification as required by the Proposed Rules (described above as step #3). This would mean that an exempt SEF – including one registered with the SEC – could not make any swaps "available to trade" under the CEA and that swaps traded only on exempt SEFs could never become subject to the trade execution mandate. This anomaly further supports the view that the Commission's proposal conflicts with the statute.

II. The Commission's Clearing Mandate Determination Should Provide Notice that a Swap is Also Subject to the Trading Mandate.

The Commission seems to appreciate that market participants will want to be able to know with certainty which swaps are subject to the clearing mandate and trading mandate. No one is well served by ambiguity concerning the application of a statutory mandate to particular swaps or to market participants that trade those swaps. The Commission is correct to try to provide that certainty. We believe the CFTC's clearing mandate determination offers the best place for the agency to set out whether a swap is subject to the clearing and trading mandates.

A. When Making the Clearing Mandate Determination for a Swap, the CFTC Should Consider The Actual or Potential Liquidity of Trading in the Swap.

As discussed above, only swaps subject to the clearing mandate can become subject to the trade execution mandate; thus, the status of a swap being "made available to trade" is only legally meaningful once the CFTC has decided that the swap must be cleared. Before the CFTC makes that decision, it must consider whether that swap has, among other things, significant

[8] The statutory text of CEA § 2(h)(8) is provided above in footnote 4.

outstanding notional exposures, trading liquidity, and adequate pricing data. In that context, the CFTC could state that the trading mandate will also apply to the swap due to existing or future trading on a SEF (if the swap is available to trade on a SEF). The clearing mandate determination will require the CFTC to consider liquidity in the swap and to make certain that market participants know whether the swap is subject to the trading mandate.

We expect only a small portion of the 500 broad-based index CDS that are available today on our platform to become subject to the clearing (and by extension, the trading) mandate. Based on information available from the Depository Trust & Clearing Corporation, during the first five weeks of 2012, seven CDS index contracts accounted for 91% of the trading volume in CDS that would be subject to the CFTC's jurisdiction.[9] When the CFTC considers which CDS will be required to be cleared, the universe of highly liquid CDS that are eligible to become subject to the clearing mandate could reasonably be expected to be limited to these seven swaps. To the extent the CFTC finds each of the seven swaps to be sufficiently liquid to be required to be cleared (and otherwise appropriate) to become subject to the clearing mandate, the swaps should also become subject to the trading mandate.

We know some commenters will express concerns that in the absence of an affirmative CFTC-driven "made available for trading" determination, market liquidity will be adversely affected because some swaps that are subject to the clearing mandate will not be traded in SEF markets with the depth and liquidity of many exchange markets. This concern is overstated. Swaps that are infrequently traded, yet subject to the trading mandate, may be traded on or through the rules of a SEF in compliance with the trading mandate if the swaps are executed in accordance with the SEF's block trading rules. These rules will allow many swaps to be executed privately and bi-laterally so long as the block trading requirements in the SEF's rules are met. As long as the SEF block trading rules are allowed to be robust, and nothing in the statute suggests they should not be, swap market participants should be able to avail themselves of flexible execution standards and resulting trading liquidity without forcing SEFs to run the gauntlet of a prolonged and duplicative made available to trade process.

B. The CFTC Should Require SEFs to Satisfy A Simple MAT Notification Process.

If the Commission wants a SEF to trigger the MAT process, once a swap becomes subject to the clearing mandate, a simple notice reciting that under the SEF's rules the swap is "made available to trade" should be sufficient. The SEF and CFTC can then post the notice on their respective websites to ensure that market participants are aware that the trading mandate will apply to the swap. Consistent with the Commission's application of the clearing mandate, the CFTC could give market participants a grace period of some appropriate time – 30 or 60 days generally might be sufficient – to comply with the trading mandate.

To maximize clarity and minimize burden on market participants, a SEF that makes any swap available to trade could be required to maintain on its website a running list of all the swaps

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[9] These seven CDS index contracts are: CDX.NA.IG.17; CDX.NA.IG.9; CDX.NA.HY.17; CDX.NA.IG.16; CDX.NA.HY.10; CDX.NA.HY.9; and CDX.EM.16.

the SEF makes available to trade. The CFTC could then post the running list of all swaps each SEF makes available to trade in one dedicated place on the CFTC's website, alongside a list of all the swaps the CFTC has required to be cleared.

MarketAxess intends to make available for trading every CDS that the CFTC determines is subject to the clearing mandate. Once the CFTC determines a CDS is subject to the clearing mandate, MarketAxess would provide notice to the CFTC that the swap is "made available to trade" on the MarketAxess System. MarketAxess would provide market participants with notice of the made available to trade status by posting this notice on its website, along with a running list of all the swaps that MarketAxess makes available to trade.

C. The CFTC should Address the Loss of Liquidity of a Swap that is Subject to the Clearing and Trading Mandate Through the Clearing Mandate.

If a swap becomes substantially less liquid after the CFTC determines the swap should become subject to the clearing mandate, the CFTC should reevaluate whether the swap should continue to be required to be cleared based on the same statutory factors the CFTC must consider when initially determining the swap is required be cleared,[10] including whether the swap has significant outstanding notional exposures, trading liquidity, and adequate pricing data. The Commission's stay procedures for the clearing mandate could be utilized to initiate this process. If the CFTC determines the swap is no longer sufficiently liquid, the CFTC should lift the clearing mandate for the swap. Once the swap is no longer subject to the clearing mandate, the swap would no longer be subject to the trade mandate either.

III. A Recognition and Notification Process Would Use CFTC and SEF Resources More Efficiently Than the Proposed Rules.

A. Embedding the CFTC's Notice of Liquidity in the CFTC's Clearing Determination Process Would be Much More Efficient than the Proposed Rules.

i. No Resources Should be Spent Clarifying whether a Swap is "Made Available to Trade" Until the Swap Is Required to be Cleared.

The simple recognition and notification process we recommend would not require the CFTC or SEFs to spend any resources regarding whether a swap is made available to trade before the CFTC determines to require the swap to be cleared. This is appropriate because a swap's legal status as being "available to trade" has no significance (and cannot trigger the trading mandate) until the swap is required to be cleared.

But the CFTC's Proposed Rules are completely divorced from the clearing mandate and would require each SEF that lists a swap that another SEF determines to "make available to trade" to undergo an onerous process that would tie up significant CFTC and SEF resources –

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[10] *See* Dodd-Frank § 723(a), adding CEA § 2(h)(2)(D); *See also* Process for Review of Swaps for Mandatory Clearing, 76 Fed. Reg. 44464 (July 26, 2011).

regardless of whether the swap is subject to the clearing mandate. This is also true for any swap listed by a SEF that is economically equivalent to a swap another SEF makes available to trade, a particularly odd result.

The Commission has not decided whether a clearing mandate it issues for one swap would apply to economically equivalent swaps. Yet the Commission's proposal would purport to make the trading mandate applicable to a swap that is economically equivalent to another swap that a SEF's competitor makes available to trade. The statute, however, makes clear that the trading mandate only could apply to a swap that is subject to the clearing mandate. CEA §2(h)(8). The Commission's proposal therefore would require SEFs to make a filing and a certification of made available to trade status for economically equivalent swaps that are not subject to the clearing mandate and therefore can not by law be subject to the trading mandate. The Commission should at least withdraw this aspect of its proposal.

ii. The Proposed Rules Would Require the CFTC to Replicate Work Already Required by Dodd-Frank and CFTC Rules.

Our alternative proposal is rooted in the fact that the CFTC is already required by law to review whether a swap has, among other things, significant outstanding notional exposures, trading liquidity, and adequate pricing data before the swap may become subject to the clearing mandate and (by extension) the trade execution mandate. There is no need to require the CFTC to take a second look at a swap the CFTC has already considered under the liquidity standard for clearing. The second look at each swap that is contemplated under the Proposed Rules would unnecessarily require a significant expenditure of the CFTC's valuable, limited resources.

iii. The CFTC's Review of SEF Determinations to Make a Swap Available to Trade Would Not Provide Added Protections.

MarketAxess appreciates the opportunity to respond to the CFTC's question whether the information that the Proposed Rules would require to be submitted to the CFTC by SEFs would have practical utility. *See* Proposed Rules at 77735. The Proposed Rules would require a SEF to consider the seven enumerated factors and any other factor the SEF considers relevant, as the SEF considers appropriate. The CFTC notes that "[n]o single factor would be dispositive, as the [SEF] may consider any one factor or several factors to make a swap available to trade." *See* Proposed Rules at 77732.

Put plainly, the CFTC delegates discretion to the SEF as to what factors are considered and how the factors considered are weighed. It is unclear how the CFTC could find that a determination made by a SEF to make a swap available to trade is somehow inappropriate or incorrect, provided that the SEF follows the basic process set forth in the rules and considers at least one factor the SEF deems to be relevant. If the CFTC lacks the ability to overturn a determination made by a SEF, the CFTC's review of the plethora of SEF determinations would have no impact on whether a swap determined by a SEF to be "available to trade" would become subject to the trade execution mandate.

B. The Suggested Simple Notification Process Is Workable for SEFs and Would not Require an Unwarranted Expenditure of SEF Resources.

Our alternative would provide clarity and certainty to market participants without tying up significant SEF resources on reports and assessments whose need has not been demonstrated. The CFTC states that the Proposed Rules are "intended to facilitate [SEFs] to make swaps available to trade, which is expected to promote the trading of swaps on [SEFs] and competition among these entities." *See* Proposed Rules at 77736. But under the Proposed Rules, SEFs would need to allocate substantial resources to make the many determinations and file the many requisite submissions and annual assessments. Imposing unwarranted costs on SEFs may create barriers to entry that prevent entities intending to register as SEFs from ultimately becoming SEFs. Fewer SEFs would mean qualified market participants have less choice in regulated trading platforms. This result would be inconsistent with the intent of the CFTC and a key goal of Dodd-Frank—to promote the trading of swaps on SEFs. Dodd-Frank §733, adding CEA § 5h(e).

C. The Proposed Rules' Use of "Economically Equivalent Swaps" Is Inconsistent with Existing CFTC Rules and the Goal of Legal Certainty.

The Proposed Rules use the term "economically equivalent swap," which does not appear anywhere in Dodd-Frank's provisions applicable to the clearing or trading mandate. Proposed Rules 37.10(c)(2) and 38.12(c)(2) loosely define this term to mean a swap that the SEF determines to be "economically equivalent" with another swap after considering each swap's material pricing terms. The term "economically equivalent swap" also appears in the position limit rules adopted by the CFTC last October and is defined differently there. Using a single term in different CFTC rules in a way that defines the same term differently would lead to confusion and legal uncertainty. As correctly noted by the CFTC staff at the January 30, 2012 roundtable regarding the Proposed Rules, the term "economic equivalent" should not be used in this manner.

We look forward to working with the CFTC to achieve the Congressional objective of promoting swap trading on SEFs. If you have any comments or questions about our comment letter or the SEF issues generally, please contact me or our General Counsel, Chuck Hood, at (212) 813-6053.

Respectfully,

Richard M. McVey
Chairman and Chief Executive Officer
MarketAxess Holdings Inc.