Pierpont
HOLDINGS

15 May 2012

Via Electronic Upload (http://comments.cftc.gov)

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

Re: **RIN 3038 – AD08**, Proposed Rule under the *Commodity Exchange Act*, as amended, ("CEA") – §§ **43.2, 43.4 & 46.6**, *Procedures to Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades* (the "**Proposed Release**")

Dear Mr. Stawick,

Pierpont Securities Holdings LLC on behalf of itself and its wholly-owned subsidiaries (including Pierpont Securities LLC, a privately-owned broker-dealer that is registered under the Securities Exchange Act of 1934, as amended, and is a member of the Financial Industry Regulatory Authority and the National Futures Association, and Pierpont Derivatives LLC (collectively, "**Pierpont**")) is pleased to submit comments on the Proposed Release as the Commodity Futures Trading Commission (the "**Commission**") establishes the regulatory framework in connection with Title VII of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, particularly §§ 727 thereof ("**Dodd-Frank**").

Cognizant of the monumental task with which the Commission has been charged, Pierpont has appreciated the Commission's adherence to certain core and guiding principles found in Dodd-Frank, including fair-and-open access ("all to all"), greater inclusiveness of and more competition among participants, transparency, liquidity and reduction of systemic risk in the "swaps" market. Unlike many other financial institutions that have commented on the Proposed Release, Pierpont is a new entrant to the swaps market and provides, it is hoped, another perspective for the Commission's consideration.

By way of background, in creating § 2(a)(13) of the CEA, §727of Dodd-Frank authorizes promulgation by the Commission of regulations to address the real-time reporting of swap-transaction and pricing data "as it deems necessary" in order " to enhance price discovery." Such

281 Tresser Boulevard, 9th Floor | Stamford CT 06901 | PHONE: (203) 428-2500 | FAX: (203) 428-2501

regulations will also apply to any outsize or large notional swap transaction, which would fall under one of two identified categories: a "block trade"[1] and a "large notional off-facility swap"[2] (each a "**Block Swap**"). With respect to any Block Swap, the Commission is charged with specifying (i) the criteria for particular markets and contracts and (ii) the appropriate time delay for reporting any such block trade publicly. As the Commission and many swaps-market participants are keenly aware, the need to balance the competing interests of anonymity, transparency and liquidity for Block Swaps, in particular, requires careful consideration.

While Pierpont favors straight-forward and readily-intelligible regulations, any "one-size-fits-all" approach is not sufficient to capture the characteristics of different asset classes and their swaps, including the trading frequency, volume and liquidity of such swaps. With respect to any Block Swap that is an interest rate swap, the instrument or product type (*e.g.*, a bullet fixed-floating swap as opposed to a basis swap) will dictate the availability of any hedge before the required data of such Block Swap are publicly disseminated.

Based on recent conversation with members of the Commission's staff, Pierpont agrees that enhanced price discovery may be attained by providing interest rate swaps data on standard tenor swaps transactions across various tenors of the swaps curve, so that swaps market participants may use these data (or "points") on the curve to build their own full swaps valuation curves. While differences exist, curve building and interpolation methodologies between key input points are fairly consistent across the industry. Dissemination of key input points across the entire interest rate swaps curve would provide all swaps market participants the benefit of information currently unavailable, except with respect to the inter-dealer market. Based on the analysis conducted by the Commission's staff on available interest rate swaps data, approximately 50 percent of interest rate swaps were between buyers and sellers who were both identified as G-14 banks. The data of these dealer-to-dealer interest rate swaps with standard tenors would form the basis for providing transparency across the swap curve for the greater market.

Historically, the over-the-counter ("OTC") interest rate swaps market has allowed for customization based on the requirements of counterparties. That said, the bulk of interest rate swaps in the market occur as standard 2 day "spot" settlement and maturities, on standard market conventions and terms, and unlike the cash securities and futures markets, a standard "spot" settle and maturity swap ("**Spot Swap**") done one day is not completely fungible with a transaction done on another day. For swap dealers and other active swaps market participants, the date specific nature of standard "spot" settled and maturity interest rate swaps leads to large portfolios of transactions, portfolios that have hedges but with slightly different dates as to settlements and maturities. For swaps dealers and other large interest rate swaps market participants, swaps compression (*e.g.*, through services offered by TriOptima AB), has been a ready solution. For less active and smaller swaps market participants, the attendant issues of mismatched hedges are managed by terminating any existing "dated" interest rate swap ("**Dated Swap**") on its specific terms instead of transacting on new, like-risk Spot Swaps.

---

[1] As defined § 43.2, a publicly reportable swap that (i) is listed on a swap execution facility ("**SEF**") or designated contract market ("**DCM**"); is traded away from the trading system or platform of a SEF or DCM but is executed pursuant to the rules and procedures of a SEF or DCM; (iii) has a notional at or above a minimum block applicable to such swap; and (iv) is reported subject to the rules and procedures of a SEF or DCM and permitted time-delay requirements.

[2] In pertinent part and as distinguished from a "block trade," a swap that is not executed pursuant the rules and procedures of a SEF or DCM.

281 Tresser Boulevard, 9th Floor | Stamford CT 06901 | PHONE: (203) 428-2500 | FAX: (203) 428-2501

In light of the nuances specific to the OTC interest rate swaps market, Pierpont asks the Commission to consider Block Swap thresholds that would not hamper liquidity in any Dated Swap by relying on Spot Swap data predominantly. Even though the Notional Amount Calculation method does take into account all types of swaps in the data pool, the weighted average is likely skewed by the higher volumes and frequency of any Spot Swap – a situation that leaves any Dated Swap under a skewed threshold. Other proposed measures of market liquidity such as market depth and breadth ignore the illiquidity of any Dated Swap.

As SEFs develop in the interest rate swaps market, Block Swap thresholds should be tailored to prevent any potential bifurcation of liquidity for any Dated Swap. As SEF Spot Swap trading pools build liquidity, care should be taken to allow for flexibility to negotiate any Dated Swap *via* block trades. Any one-size-fits-all threshold would result in swap users paying wider bid/offer for specificity *via* Request for Quote to a smaller pool of market makers, or would encourage swap users to take undue risk by transacting in the deeper liquidity pool of the Spot Swap market. The net effect would be to push off trade compression to larger, less frequent exercises and force swap users to warehouse compression risk and increase the number of outstanding (or "off-the-run" or "back-contract") interest rate swaps in the market.

The Notional Amount method for calculating an applicable threshold introduces a bias that could result in risks of liquidity for any Dated Swap. The Commission may consider analyzing data by separating the Spot Swap data from those Dated Swap data, being mindful to leave no room for swaps market participants to circumvent the core and guiding principles found in Dodd-Frank. Pierpont suggests that the Commission adhere to its current swaps categories to preserve simplicity; however, the Commission should consider using a Notional Amount Calculation lower than the proposed 67% to allow swaps market participants flexibility to manage portfolios in a liquid and prudent manner. Without an ability to analyze the actual data, Pierpont contends that a Notional Amount Calculation of 50% or less be relied on in order to strike a better balance between anonymity, transparency and liquidity.

Additionally, Pierpont suggests that, for any interest rate swap where one counterparty is not a registered Swap Dealer, the same swaps categories for simplicity and consistency be used, but the Commission allow a for a lower Block Swap threshold using a Notional Amount Calculation of 25%. The additional protection of liquidity for any non-Swap Dealer would shift the burden of transparency to Swap-Dealer-to-Swap-Dealer interest rate swaps, a burden better suited to those who hold themselves out as market makers.

On behalf of Pierpont, my colleagues and employees, I thank you for the opportunity to submit comments on the Proposed Releases.

Sincerely,

Mark B. Werner
Chief Executive Officer &
Member of the Board of Managers