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IHS Markit

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW,
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March 15, 2019

Re: Swap Execution Facilities and Trade Execution Requirement, Notice of Proposed Rulemaking, 83 Fed. Reg 61,946 (Nov. 30, 2018)

Dear Mr. Kirkpatrick,

IHS Markit is pleased to submit these comments in response to the Commodity Futures Trading Commission's ("Commission") notice of proposed rulemaking concerning "Swap Execution Facilities and Trade Execution Requirement."

IHS Markit is a global information and services company that provides data, insight, and solutions across 17 industries.[1] IHS Markit is a NASDAQ-listed public company under the ticker "INFO." IHS Markit has approximately 15,000 employees in 35 countries, including over 5,000 employees in the United States with offices in 21 states and the District of Columbia.

IHS Markit's Financial Services division accounts for just over one-third of IHS Markit's revenues[2] and provides data, software, technology platforms and managed services designed to address a variety of financial services industry-related challenges.[3] IHS Markit's derivatives trade processing platform, MarkitSERV, is an important business within the Financial Services division. The derivatives trade processing platform facilitates connectivity and interaction between swap dealer, buyside, fund administrators, and corporate end-user market participants and derivatives market infrastructures including, most importantly for the purpose of this comment letter, swap execution facilities (SEFs).[4] Among the specific services

[1] For more information regarding IHS Markit's solution offerings for these 17 industries, please see https://ihsmarkit.com/products.html.

[2] See IHS Markit, SEC Form 10-K Filing (Jan. 18, 2019).

[3] See IHS Markit Financial Services, https://ihsmarkit.com/industry/financial-markets.html.

[4] See MarkitSERV, https://ihsmarkit.com/products/markitserv.html.

offered by MarkitSERV are trade confirmation, trade affirmation, submission of matched (confirmed or affirmed) trades to clearing, as well as a standard connectivity solution with customer risk offices. IHS Markit's derivatives trade processing services also help facilitate compliance with swaps reporting and confirmation requirements, among other regulatory requirements, in addition to facilitating clearing, providing operational efficiencies and mechanisms for risk mitigation.[5] Globally, over 2,500 firms, 15 central counterparties, and over 70 execution venues use IHS Markit's derivatives processing platform which processes, on average, 90,000 swap transaction events every day.

I. Executive Summary

We commend the Commission's expansion of the potential suppliers of regulatory services for SEFs under the proposed § 37.204(a) because it will reduce the start-up and operating costs of operating a SEF. We also applaud the introduction of the prompt, efficient, and accurate standard for the straight-through processing (STP) of swaps subject to the trade execution requirement as better reflecting the manual realities of processing trades with a voice execution component.

We question, however, the elimination of the "made available to trade" (MAT) standard applied to swaps subject to the clearing requirement in order to determine their eligibility for the SEF trade execution requirement because it would increase costs for trading such illiquid swaps without commensurate transparency or liquidity benefits. Instead of eliminating the MAT standard, we would urge the Commission to revise it to align more closely with the approach taken by European regulators for their Trading Obligation.

II. Comments

a. Comments on Specific Proposed Regulations

1. Proposed § 37.204(a) and Regulatory Service Providers

We commend the proposed § 37.204(a), which provides that:

Use of regulatory service provider permitted. A swap execution facility may choose to contract with a registered futures association or another registered entity, as such terms are defined under the Act, or any non-registered entity (collectively, ''regulatory service providers''), for the provision of services to assist in complying with the Act and Commission regulations thereunder, as approved by the Commission. […]

[5] See MarkitSERV for EMIR Reporting, https://www.markitserv.com/assets/ms-en/docs/presentations/MarkitSERV_for_EMIR_Regulatory_Reporting_presentation.pdf.

Proposed § 37.204(a) represents the Commission's embrace of the new paradigm in financial services: the modular delivery of services and the core understanding that platforms, like a SEF, represent a bundle of services. Some services delivered by a SEF are differentiating, e.g., customer relationships, methods of execution, etc. Other services are non-differentiating and result in little to no competitive value except when delivered at the lowest possible cost, e.g., recordkeeping, audit trail, surveillance. Proposed § 37.204(a) encourages vendors to develop non-differentiating services for SEFs, resulting in more options (buy vs. build) for SEFs and lowering the start-up and ongoing costs associated with launching and operating a SEF. In this way, Proposed § 37.204(a) is a pro-competitive regulatory change that should further the central aims expressed in the overall rulemaking package of making SEFs more dynamic, innovative, and competitive.

More specifically, we would urge the Commission to clarify the process and standards governing Commission approval of third-party regulatory service providers. First, we recommend that the Commission allow third-party regulatory service providers to obtain approval to provide regulatory services *before* they are retained by a SEF, i.e. pre-approval. This could be done through the submission of a Form SEF, filled out in pertinent parts. A pre-approval process would encourage third-party fintech and regtech service providers to develop regulatory services for SEFs on spec, increasing the supply of such service providers and thereby reducing costs for SEFs.

Second, we would further urge the Commission to ensure that the process and standard for a third-party regulatory service provider to receive approval and the process for a SEF to obtain approval for an in-house regulatory service both be subject to the same standards and diligence, ensuring that neither third-party services nor in-house solutions receive Commission or Commission staff preferential treatment.

2. Proposed § 37.2(b) and the Trade Execution Requirement

We urge the Commission to preserve the Made Available to Trade (MAT) requirements in § 37.10 and revise it in a future rulemaking to align more closely with the European Securities and Markets Authority (ESMA)'s approach to the trading obligation.[6] Specifically, we would urge the Commission to apply a liquidity test before the Trade Execution Requirement is applied to a new swap contract listing. This liquidity test should be developed in consultation with the

[6] Final Report, Draft RTS on the trading obligation for derivatives under MiFIR, ESMA70-156-227, https://www.esma.europa.eu/sites/default/files/library/esma70-156-227_final_report_trading_obligation_derivatives.pdf (Sept. 28, 2017). See also our comment letter to ESMA on the proposed RTS, https://cdn.ihs.com/www/pdf/IHS-Markit-response-ESMA-CP-Trading-Obligation-Jul-2017.pdf (July 2017).

public after a substantial notice and comment period.

Aligning the Commission's approach with ESMA would also reduce the commercial and policy costs associated with divergent approaches to the Trade Execution Requirement between Europe and the United States. As a post-trade service provider for a large proportion of SEF and off facility swaps subject to MAT and not subject to MAT, we question the value of extending the Trade Execution Requirement potentially to all swaps subject to the Clearing Requirement. Swaps subject to the Clearing Requirement but not currently subject to the Trade Execution Requirement are illiquid and as such do not benefit from centralized SEF trading and any pre-trade transparency such trading could bring (particularly without an RFQ 3 requirement). Moreover, any post-trade processing benefit of trading on a SEF is fully obviated by the use of MarkitSERV or other electronic processing platforms, which is the norm for less liquid swaps subject to the clearing requirement.

If the Commission mandates the use of a SEF for the execution and processing of currently non-MAT, illiquid swaps subject to the Clearing Requirement, it will raise the cost of trading by requiring the payment of new fees to a SEF with no discernible benefit in terms of additional pre-trade transparency or potential, even theoretical, of generating new market liquidity. These increased costs without commensurate benefit would also reduce the value proposition post-trade processing service providers can offer.

b. *Comments on Specific Requests for Comment Questions*

(14) Is the proposed six-month delay period sufficient to allow swaps broking entities, including interdealer brokers, time to seek registration or alter their operations in compliance with the SEF registration requirements? Why or why not?

Given the extensive changes this rulemaking would make to the operation of SEFs and the swaps trading and market structure more generally, we would advise a transition period of 12 months or more. This additional time would, among other things, allow new fintech regulatory service providers and other service providers to develop, test, gain CFTC approval, and market new services that would reduce the costs associated with building and operating a SEF. Without this extended transition period, new SEFs would have fewer options to build these non-differentiating services themselves or obtain them from a constrained market of such services. These fixed costs would deter or delay the entry of new competitors into the market for SEF services and benefit incumbents, blunting the Commission's goals of promoting responsible innovation and fair competition.[7]

[7] See CEA section 4(c) and 83 Fed. Reg. 61,946, at 62,037.

(20) Should the Commission require a SEF to include a minimum set of terms in a trade evidence record, e.g., material economic terms? Should the Commission specify those terms in the proposed regulation?

We would advise that the Commission to require that SEFs include the disclosure of all "material economic terms" as a minimum. The reason for requiring disclosure of all such terms is to for the purpose of ensuring that SEFs satisfying their "trade evidence record" disclosure requirement. The "material economic terms" could be defined as those terms that would be necessary to price, settle, or calculate or make payments for an uncleared swap.

(23) Should the Commission specify in its regulations that notwithstanding the trade evidence record requirement, a SEF is allowed to incorporate by reference underlying, previous agreements containing terms governing a swap transaction into any trade evidence record associated with the transaction?

Yes. Allowing a SEF-executed trade the ability to incorporate by reference underlying and previous agreements is absolutely critical to ensuring continuity between current SEF operations and SEF operations following the conclusion of this rulemaking.

(27) Should the Commission define ''as soon as technologically practicable'' in a similar manner to the definition in part 43?

We would support aligning the definitions of "as soon as technologically practicable" across the Commission's regulations where the standard is appropriate, i.e. where the process is an automated process driven solely by technology. The definition in part 43 which states that "[a]s soon as technologically practicable means as soon as possible, taking into consideration the prevalence, implementation and use of technology by comparable market participants" is a reasonable one because it reflects consensus market practices.

(35) Should the Commission allow an exception to the proposed prohibition against pre-execution communications for all corrective trades intended to resolve error trades pursuant to the proposed error trade policy rules under § 37.203(e), as discussed further below? Please explain why or why not.

We would encourage the Commission to include an exception to the proposed prohibition against pre-execution communications for communications related solely to corrective trades. These communications do not lead to new, price-forming trades but are instead clerical in nature. The submission of corrective trades often involve middle and back office staff that do not have access to a SEF's systems. Requiring error trade negotiations to happen on SEF would impose unnecessary costs on both market participants and SEFs, thereby reducing SEF trading volume.

We understand that the Commission would have concerns that exempting communications related to corrective trades from the SEF pre-trade communication requirement would create a potential loophole and weaken the SEF trading requirement. We would note that such trades would be flagged and SEFs and the Commission could perform establish rules against misusing this exemption and perform surveillance and enforce violations.

(46) Does the lack of a void ab initio requirement for non-credit related errors create concerns about market risk with respect to error trades that have been executed, but have not been voided despite the rejection from clearing? If so, should a SEF be limited in the types of errors that may be corrected without void ab initio, e.g., errors that do not create market risk? Should the Commission adopt a mandatory void ab initio requirement that certain types of errors, e.g., those that do cause market risk, must be resolved via a corrective trade approach? Or should counterparties otherwise have the ability to maintain breakage agreements to address such risks?

We would disagree that the "lack of a void ab initio requirement for non-credit related errors create[s] concerns about market risk." To the contrary, the void ab initio rule creates market risk, as it forces parties to an error trade to absorb the market risk from the intended time of execution to the time a new trade is executed.

(49) Should trades that are rejected by a DCO for insufficient credit be required to be deemed to be void ab initio by SEFs? If so, should the Commission codify such a requirement under proposed § 37.203(e) or elsewhere in the Commission's regulations?

In theory, because of pre-trade credit checks we would expect the population of trades rejected by a DCO for insufficient credit would be limited. We would caution that a rule that provides. that trades rejected by a DCO for insufficient credit be limited to only instances where an actual credit limit was rejected based on the intended economics of the transaction and not due to an error in the economic terms of the swap that led to a credit rejection.

(52) Should a SEF be permitted to adjust or cancel an error trade without consulting with the parties to the trade in some or all circumstances, or should the Commission require a SEF to consult with or obtain the consent of the parties to an error trade in some or all circumstances?

If the source of the error is entirely the SEF, then SEFs should have discretion to correct their own error, provided that prompt and reasonable notice is provided to all parties that a correction was made.

(53) Should market participants be required to report all errors to a SEF or are there certain errors that are immaterial and do not otherwise require correction?

Some errors are immaterial and do not affect the economics of a transaction, e.g., allocation details, broker/SEF trading professional details, brokerage amount, trader name, etc. For such immaterial and non-economic trade details, there should be no specific requirement to report such errors or if such a requirement exists. Instead, such mandatory reporting should be limited only to those instances where the party becomes aware of them.

(57) Should the Commission require SEFs to notify all market participants of an error trade and the resolution of such trade or only a smaller subset of participants? Should the Commission provide any time frame for such notice?

We would only recommend that SEFs be required to notify all market participants of an error trade and the resolution of such trade a requirement for error trades whose errors manifested in the real-time public reporting record related to the transaction. Such notice should be provided as soon as practicable after correction of the error trade is made.

(58) Should a DCO be required to notify a SEF of the reason why a trade was rejected from clearing? If so, what type of information should the Commission require the DCO to provide to the SEF in such a circumstance?

DCOs should be required to promptly notify the SEF as to the reason a trade was rejected for clearing. Such notifications would facilitate correction of the trade.

(71) The proposed ''prompt, efficient, and accurate'' standard, as applied to trades submitted to a DCO for clearing via third-party affirmation hubs would take into consideration evolving swap market practices and technology, as well as current market conditions at the time of execution. Is the proposed approach appropriate? Why or why not? Does the approach provide sufficient guidance regarding the standard?

We commend the use of the "prompt, efficient, and accurate" (PEA) standard for the submission of swaps by a SEF to a clearinghouse. The PEA standard better describes the optimal process for routing all SEF swaps, voice or electronic, to clearing and recognizes the balance between these sometimes countervailing concerns that is the basis of affirmation review of a SEF's manual entry of a swap's terms.

In contrast the "As Quickly As Technologically Practicable As if Fully Automated Systems are Used" standard for processing and routing of SEF transactions conflicts with existing and prudent practice for the post-trade processing of voice SEF trades.

Processing of voice trades necessarily includes two steps of mostly manual intervention: (1) at trade detail entry, i.e. the SEF's manual entry of trade details based on parties' agreement and (2) at affirmation, i.e. the point where these trade details are reviewed and affirmed for accuracy. The "As Quickly As Technologically Practicable As if Fully Automated Systems are Used" implies that only automated processes should apply after a trade is executed and as the trade is routed to clearing, i.e. no non-automated systems can nor should be used.

We stress that we do not think the adoption of the PEA standard will result in a "race to the bottom" in terms of affirmation times. Firms are incentivized by prudent risk management standards and the PEA standard itself to ensure prompt affirmations. Indeed, the Commission's clearly stated expectation is that market participants and affirmation hubs will continually improve on their post-trade processes.[8] To further ensure its intentions are realized, the CFTC could include in a preamble describing a final rule language that states something to the effect of: "the Commission clarifies that firms that trade on SEF should always strive to invest in people and technology that would enable them to balance all three principles conveyed by the PEA standard. Firms will not meet the PEA standard if they strive to meet one principle and not others, e.g., by developing post-trade processes designed only for ensuring accuracy and not promptness and efficiency."

The Commission could also help market participants seeking to ensure timely affirmation times by requiring SEFs to disclose median bilateral affirmation times and requiring SEFs to monitor compliance with the PEA standard by using this disclosed median affirmation time as a guideline (but not as a mandatory standard). The disclosure of this median affirmation time can also encourage self-policing of prompt affirmations, e.g., if party A has affirmed within this disclosed median affirmation time but party B hasn't, party A could refer to the disclosed median affirmation time to apply pressure to party B to affirm.

We also note that the Commission should clarify in any final rulemaking or guidance that affirmation hubs play no role in SEFs' and market participants' specific processing time requirements. In the Proposal, the Commission "observed that many SEFs, particularly those that offer voice-based or voice-assisted trading systems or platforms, *have not been able to meet the time frame when using manual affirmation hubs*."[9] Specific processing time requirements may not be met not because of the use of affirmation hubs, but because of the risk and complexity of ensuring that a voice-based or voice-assisted trade has been accurately entered by the relevant SEF through the manual affirmation process.

[8] The Commission states "expects that market and technological developments will enable processing and routing through affirmation hubs to occur in increasingly shorter time intervals." Id. at 62,022.

[9] Id. at 62,022.

(72) Is the distinction sufficiently clear between (i) the submission and related processing and routing of a swap by a SEF to a DCO under the "prompt, efficient, and accurate" standard and (ii) the DCO's decision to accept or not accept a swap under the AQATP standard? Does the approach provide sufficient clarity regarding the distinct, but interrelated, roles of SEFs and DCOs? Why or why not?

We think the distinction is clear. On a related point, we recommend that the Commission clarify that the need for the PEA standard isn't necessarily a consequence of the use of an affirmation hub, but of manual processes needed to ensure the accuracy of transaction processing. In contrast, the process for DCO's decision to accept or not accept a swap for clearing is an automated process, based on the DCO's clearance logic and would not require manual processes to ensure accurate clearance and settlement.

III. Conclusion

In any future final rulemaking or re-proposal, we would urge the Commission finalize the proposed expansion of the potential suppliers of regulatory services for SEFs under the proposed § 37.204(a) because it will reduce the start-up and operating costs of operating a SEF. We would also encourage the adoption of the PEA standard for the STP processing of swaps for clearing subject to the trade execution requirement as better reflecting the manual realities of processing trades with a voice execution component. We would urge the retention and improvement of the MAT standard applied to swaps subject to the clearing requirement in order to determine their eligibility for the SEF trade execution requirement because it would increase costs for trading such illiquid swaps without commensurate transparency or liquidity benefits.