WMBA
AMERICAS
WHOLESALE MARKETS BROKERS' ASSOCIATION

March 15, 2019

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Swap Execution Facilities and Trade Execution Requirement (RIN 3038-AE25)

Dear Secretary Kirkpatrick:

The Wholesale Markets Brokers' Association, Americas ("WMBAA")[1] appreciates the opportunity to provide comments to the Commodity Futures Trading Commission ("CFTC" or "Commission") in response to the Commission's proposed rules governing swap execution facilities ("SEF") and the trade execution requirement (the "Proposed Rule").[2] The WMBAA generally supports this rulemaking that appears to better align the Commission's rules regulating SEFs with Congress's intent to encourage where possible and appropriate liquidity formation, price discovery, and trade execution on regulated trading platforms (i.e., SEFs) under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").

I. EXECUTIVE SUMMARY

As interdealer brokers, the WMBAA's members create and operate platforms for price discovery and trade execution across global listed and over-the-counter cash and derivatives markets. Some of those markets are naturally highly liquid and trade on a continuous basis, while others are less liquid and trade less frequently. Across asset classes, products trade in a manner that is consistent with their liquidity characteristics (i.e. number of participants, complexity of products, information available, etc.). Typically, as products move down the liquidity spectrum, the trading platform must do more work and be more flexible in its methods to generate sufficient knowledge and interest in the marketplace to arrive at the most accurate market value and an executable price for these products. A large block trade or a transaction in an illiquid product can involve significant work to develop competitive price discovery or it could involve a number of trades to work up to the desired size. During times of market stress or particular volatility, market participants are wary of simply posting executable prices for fear that the market is moving too quickly and less predictably. By

[1] The WMBAA is an independent industry body representing the largest inter-dealer brokers. The members of the group—BGC Partners, GFI Group, Tradition, and TP ICAP—operate globally, including in the North American wholesale markets, in a broad range of financial products, and have received registration as swap execution facilities. The WMBAA membership collectively employs approximately 4,000 people in the United States; not only in New York City, but in Stamford and Norwalk, Connecticut; Chicago, Illinois; Jersey City and Piscataway, New Jersey; Raleigh, North Carolina; Miami, Juno Beach, Florida; Burlington, Massachusetts; and Dallas, Houston, and Sugar Land, Texas. For more information, please see www.wmbaa.com.

[2] Swap Execution Facilities and Trade Execution Requirement, Proposed Rule, 83 Fed. Reg. 61946 (Nov. 30, 2018) [hereinafter *Proposed Rule*].

facilitating the execution of swap trades in both highly liquid and less liquid products, SEFs that offer multiple modes of trade execution can accommodate a broader array of swap trades than SEFs that offer solely electronic order book or request for quote ("RFQ") systems. Put simply, the mode of execution necessary to produce the best price for a trade is a function of the natural liquidity of the product, the frequency at which it normally trades, the size of the trade, and market conditions at the time of the trade.

The overriding goal of the trading mandate in the Dodd-Frank Act was to move as many swap transactions as possible from the unregulated market onto regulated venues. Specifically with respect to SEFs, the statute intended to create a regulatory category of swap trading venues that promote impartiality, transparency, price discovery, and competitive price formation. Further, the statute sought to ensure that mandatorily cleared swaps were traded on regulated SEFs and, as reflected in the clause "by any means of interstate commerce," did not contemplate that swaps be traded on particular types of SEFs using prescriptive execution methods. Accordingly, the WMBAA has publicly advocated for ensuring that SEF trading could be conducted through any mode of trade execution.

The existing rules, however, ignore this flexibility by limiting trading in the most liquid ("Made Available to Trade") swaps to electronic order book or RFQ functionality. The Commission's revised SEF regulatory regime should conform to Congressional intent, reflect the plain language of the statute, and permit SEFs to employ a variety of modes of execution as long as they promote liquidity, impartiality, competition, and price discovery. The WMBAA supports the Commission's efforts to take a comprehensive approach to ensuring that all aspects of the current rules are amended where necessary to ensure that there is no bias or discrimination between different types of SEF methods of execution.

The Commission also should take into consideration the significant differences between futures trading on exchanges and swaps trading on SEFs. While it may be appropriate to reference the futures model as instructive in certain instances, the current SEF rules rely too heavily on that model and do not achieve Congress' goal. Congress explicitly created a SEF alternative to the futures trading model, understanding that competitive execution platforms provide a valuable market function. The revised rules should reflect Congressional intent and promote the growth of competitive, vibrant swaps markets without impeding liquidity formation.

There are two significant, yet unfinished aspects of the Proposed Rule. First, with respect to the cross-border application of U.S. swaps trading rules, the Proposed Rule provides a two-year transition period, but any meaningful reform to the swaps execution rules must concurrently address cross-border issues. Global liquidity pools have already been bifurcated between entities that will transact with U.S. persons and those that will not transact with them, and trifurcation of certain swaps markets appears to be on the horizon as a result of Brexit. The second issue relates to the "Embargo Rule," which hampers the ability of SEFs to operate a dynamic environment and generate activity and liquidity among SEF participants. While this requirement is technically a part of the swaps reporting regime (Part 43), it is an issue that requires immediate attention.

II. THE WMBAA GENERALLY SUPPORTS THE CFTC'S PROPOSED SEF RULES

The WMBAA provides the following comments on a number of specific proposals in the Proposed Rule.

(1) SEF Registration Requirement for Swaps Broking Entities, Including Interdealer Brokers

The Commission has proposed that swaps broking entities, including interdealer brokers, that offer a trading system or platform in which more than one market participant has the ability to trade any swap with more than one other market participant on the system or platform must register as a SEF.[3] The Commission also has proposed that where an entity operates both a registered SEF and an affiliated swaps broking entity, the swaps broking entity could comply with the SEF registration requirement by integrating its non-SEF trading system or platform into its affiliated SEF. Domestically, this integration must occur within six months of publication of the final rule.

While the integration process presents rather significant burdens and costs to SEFs and their affiliated broking entities, achieving reasonable compliance with the proposed requirement is not necessarily insurmountable. The Commission should, however, recognize that swaps broking entities affiliated with registered SEFs may introduce some of their transactions to SEFs for execution, but not all of their business falls within the jurisdiction of the CFTC for purposes of SEF registration. As such, it will be necessary to establish a regime whereby a swaps broking entity's systems or platforms are able to satisfy the SEF transaction and recordkeeping requirements, while also conducting non-SEF business. For example, a swaps broking entity may arrange and introduce certain equity swaps to a SEF for execution, but also may conduct substantial business in instruments that do not fall within the CFTC's jurisdiction.

As a result, the WMBAA seeks confirmation that a broker, defined in the proposed rule as a "SEF trading specialist," who resides within the SEF for purposes of trading swaps subject to the CFTC's jurisdiction may also, if properly registered with the relevant regulator, transact in instruments that do not fall within the CFTC's jurisdiction and that are not executed on a SEF system or platform. Similarly, the WMBAA seeks confirmation that a SEF trading specialist should have the ability to route a transaction to an equivalent platform, such as an Organized Trading Facility ("OTF") or Multilateral Trading Facility ("MTF"), if requested to do so by a market participant. The WMBAA seeks further confirmation that a SEF trading specialist is allowed to route a transaction to an equivalent venue on behalf of a market participant without carrying any form of registration with another U. S. regulator. In other words, the SEF trading specialist is allowed to route transactions to equivalent venues without carrying any form of registration with the National Futures Association ("NFA").

[3] *Id.* at 61959.

(2) Cross-Border Concerns: SEF Registration Requirement, Delay of Compliance Date

With respect to cross-border concerns, the WMBAA submits that hastily considered policies might further fragment international liquidity pools and trigger unintended consequences for swap broking entities, such as requirements to register as trading venues in local markets. The WMBAA agrees with the Commission that delaying the compliance date of the registration requirement with respect to foreign swaps broking entities, including foreign interdealer brokers, that facilitate the negotiation or arrangement of swaps transactions for U.S. persons for two years should help to alleviate or at least minimize any disruptions to their operations and hopefully avoid the fragmentation of swaps liquidity observed following publication of the Part 37 rules.

Additionally, the WMBAA looks forward to a Commission determination as to what constitutes a "direct and significant connection with activities in, or effect on, commerce of the United States." The WMBAA suggests that the Commission evaluate the efficacy of the application of the SEF trading mandate as currently applied to U.S. entities as part of this determination. The Commission currently has the ability to obtain information and monitor the overseas swap trading activities of U.S. entities through its transaction reporting rules. The public policy purpose of dictating the method and the venue for U.S. entities to facilitate the negotiation and arrangement of swap transactions in markets where the greatest liquidity is off-shore is not clear.

Absent a determination with respect to the application of SEF trading rules to the non-U.S. activity of U.S. entities, the WMBAA is supportive of the proposal that eligible foreign swaps broking entities, which include foreign interdealer brokers, be able to continue to facilitate the negotiation and arrangement of swaps transactions for U.S. persons and subsequently route these pre-arranged transactions to a SEF or exempt SEF for execution.

The WMBAA believes that it is incumbent on the Commission as it evaluates the registration requirements for eligible foreign swaps broking entities to recognize the implications of requiring SEF registration for such entities. If a foreign interdealer broker affiliated with a registered SEF were required to register as a SEF, the affiliated SEF would likely seek to establish a branch office in the foreign jurisdictions that would encompass the business and personnel of the foreign interdealer broker rather than register that foreign affiliate as a separate SEF. Establishing SEF branch locations in these foreign jurisdictions is an involved and prolonged process. For example, it is the WMBAA's understanding that the Financial Conduct Authority ("FCA") in the United Kingdom would require any SEF branch office to seek registration as a Recognized Overseas Investment Exchange ("ROIE"). Upon information and belief, the process to register as a ROIE is lengthy and, as far as SEFs are concerned, would present a case of first impression to the FCA that may or may not be viewed as appropriate. Likewise, establishing SEF branch locations in the Asia Pacific region would involve registration requirements in Hong Kong, Australia, and Singapore, and would likely present the same concerns to the relevant regulatory authority as presented by the ROIE registration process. The registration process in these foreign jurisdictions would likely be lengthy, expensive, and result in duplicative or conflicting regulatory requirements with no concomitant benefit to SEF liquidity or the intended goal of the Proposed Rule. As such, the WMBAA asks that the CFTC remain mindful of these issues as it evaluates the registration requirement for foreign entities.

Further, the WMBAA suggests that the CFTC consider allowing U.S. persons transacting swaps in non-U.S. jurisdictions to execute in local markets through comparably registered foreign swaps broking entities rather than requiring foreign swaps broking entities to register as swap interdealer brokers with the NFA. This transaction flow is common in other markets. NFA registration is a costly and burdensome obligation, particularly when considering that the amount of business that foreign swaps broking entities transact with U.S. persons is generally *de minimis* in relation to the overall business of the foreign swaps broking entities and poses no "direct and significant connection with activities in, or effect on, commerce of the United States."[4]

It is the WMBAA's understanding that, during the proposed two-year delay period for registration of eligible foreign swaps broking entities, and as set forth in the Proposed Rule, the status quo for eligible swaps broking entities would be maintained. That said, and in view of the Commission's proposal to eliminate the minimum trading functionality requirement and the regulatory order book definition, the WMBAA seeks clarification that pre-arranged transactions routed to a SEF for execution by a eligible foreign swaps broking entity would need not be executed via the minimum trade functionality, but could instead be executed within the SEF facility or system via any means of interstate commerce.

(3) §§ 37.3(a)(2)-(3); 37.9 — Minimum Trading Functionality: Eliminating Required Execution Methods to Permit Multiple Modes of Trade Execution

In adopting the existing rules, the Commission required each registered SEF to have 'minimum trading functionality" under § 37.3(a)(2) such that the SEF must maintain an order book for all of the swaps that it lists for trading. An order book is defined under § 37.3(a)(3) as (i) an electronic trading facility; (ii) a trading facility; or (iii) a trading system or platform in which all market participants in the trading system or platform have the ability to enter multiple bids and offers, observe or receive bids and offers entered by other market participants, and transact on such bids and offers.[5]

The Commission is proposing to eliminate the minimum trading functionality requirement and the order book definition.[6] In addition, under the proposal, the Commission would eliminate the existing execution method requirements under § 37.9 and allow all trades that are mandatorily cleared and listed to be traded by any method of execution.[7] The Commission explained that "[a]s long as multiple participants have the ability to accept bids and offers from other multiple participants within the facility or system, the facility or system will meet the SEF definition, regardless of how the multiple participants choose to interact with one another."[8]

Since the concept of a minimal functionality requirement is inconsistent with the statute by both limiting methods of execution and, as a result, potentially limiting the number and breadth of swap

[4] *Id.* at 61962.
[5] *Id.* at 61963-64.
[6] *Id.* at 61964.
[7] *Id.* at 61980.
[8] *Id.* at 61964.

transactions that are able to be subjected to the trade execution mandate, the WMBAA strongly supports the Commission's proposal to eliminate the minimum trading functionality requirement and the order book definition. The WMBAA agrees with the Commission's conclusions and observations in justifying the proposed changes and, more importantly, believes that the proposed revisions are necessary to be consistent with the statutory requirements of the Dodd-Frank Act. The SEF definition in the Dodd-Frank Act states unequivocally that trade execution through a SEF is permitted "through any means of interstate commerce."[9] Congress was unambiguous that regulated SEFs can execute trades that are subject to the trade execution mandate through multiple modes of trade execution and clearly demonstrated its intent in the plain words of the legislative text. The Commission's existing rules, by restricting the use of voice-based systems through cumbersome processes such as the embargo rule, impairs markets that rely on voice-based or hybrid systems by hindering the creation of liquidity. Furthermore, if trades subject to the mandatory SEF trading (MAT trades) can be executed by only two methods, there is an increased risk that transactions where there is not sufficient natural liquidity for those methods will be executed away from regulated SEFs. The WMBAA agrees with the Commission that the swaps markets will be better served by allowing for evolution in trade execution functionality in line with liquidity characteristics through competition and innovation on regulated SEFs.

With this proposal, market participants would be allowed to use whatever execution methods best suit their trading needs and the swap being traded on a regulated SEF, so long as the SEF definition continues to be met. This proposal is one of many in the Proposed Rule which better aligns the Commission's regulations with the true meaning of "any means of interstate commerce."[10]

(4) § 37.6(b) – Swap Documentation Requirements for Uncleared Swaps

(a) § 37.6(b)(1) – Legally Binding Documentation

Section 37.6(b) currently requires a SEF to provide each counterparty to a transaction with a written "confirmation" that contains "all of the terms" of a swap transaction at the time of the swap's execution, applicable to both cleared and uncleared swap transactions.[11] These terms include all economic terms that are specific to a transaction, *as well as* all non-specific "relationship terms" that generally govern all transactions between two counterparties, including default provisions, margin requirements, and governing law. The term "confirmation" is defined in Parts 43 and 45 as the consummation (electronically or otherwise) of legally binding documentation that memorializes the agreement of the counterparties to all terms of the swap.

For uncleared swaps, many terms related to a transaction are negotiated and executed between counterparties prior to execution of a swap trade. The Part 37 rules thus allow SEFs to meet their §

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[9] 7 U.S.C. § 1a(50).

[10] Chairman Giancarlo put it best when he said that ". . . Title VII of Dodd-Frank permits [SEFs] to conduct their activities through 'any means of interstate commerce,' not 'such means that may be chosen by regulators.' Once regulators step in and dictate who serves who with what type of service, we are picking winners and losers. We are simply not authorized, nor are we competent, to act in this way." *Proposed Rule*, *supra* note 2, at 62140.

[11] *Id.* at 61972.

37.6(b) obligations for uncleared swaps by referencing the relevant terms in the agreement, if the individual agreement for the counterparties was submitted to the SEF prior to execution. As the Commission observed, this requirement has resulted in "high financial, administrative, and logistical burdens [on SEFs] to collect and maintain bilateral transaction agreements from many individual counterparties" such that SEFs are "unable to develop a cost-effective method to request, accept, and maintain a library of every previous agreement between counterparties."[12] Recognizing these technological and operational challenges, Commission staff has granted, with certain conditions, time-limited no-action relief such that the staff will not recommend that the Commission take enforcement action against a SEF that (1) incorporates by reference terms from previously-negotiated agreements between counterparties without first having been supplied copies of such agreements, (2) does not keep a copy of the agreements incorporated by reference in the SEF's confirmation, and (3) fails to report certain confirmation data when such data are contained solely in the terms of the underlying agreements that are incorporated by reference.[13]

Under the proposed amendments, with respect to uncleared swaps, § 37.6(b)(ii) specifies that SEFs would be required to provide to each counterparty to the uncleared swap a "trade evidence record."[14] As proposed, a trade evidence record would mean legally binding documentation that memorializes the terms of a transaction and legally supersedes any conflicting term in any previous agreement that relates to the swap transaction. The Commission noted that a trade evidence record need not include all of the terms of the transaction, including relationship terms in the underlying documentation, but should include, at a minimum, the "economic terms" that are agreed upon between the counterparties to a specific SEF transaction, e.g., trade date, notional amount, settlement date, and price. The Commission believes that the proposal is a more practical and simplified approach that would meet the legal documentation requirements, provide SEF participants legal certainty, and accommodate existing counterparty trading practices for uncleared swaps.

The WMBAA supports these proposed changes, but believes information provided by a SEF on a trade evidence record should be limited to "economic terms." The WMBAA appreciates the Commission's practical approach that a SEF trade evidence record should reflect the terms of a trade that the SEF has access to and control over. A SEF trade evidence record (that could possibly be re-termed as a "transaction acknowledgement") should be written documentation (electronic or otherwise) that includes the economic terms of the trade agreed to by the counterparties on the SEF and legally supersedes any conflicting terms of previously-negotiated agreements between the counterparties.

(b) § 37.6(b)(2) – Requirements for Swap Documentation

Section 37.6(b) generally requires that the confirmation to counterparties of a swap transaction take place at the same time as execution.[15] The Commission is proposing to amend this provision in

[12] *Id.*
[13] *Id.* at 61972-73.
[14] *Id.* at 61973.
[15] *Id.*

proposed § 37.6(b)(1)(ii)(B)(2) by requiring SEFs to provide a confirmation document or trade evidence record to the counterparties "as soon as technologically practicable" after the execution of the swap transaction on the SEF. The Commission stated that it "recognizes that a strict implementation of the existing requirement is not practical from a temporal standpoint, given that a SEF's issuance of a written confirmation document or trade evidence record would only occur upon execution by counterparties," and that simultaneous issuance of a written confirmation or trade evidence record may be impracticable from an operational and technological standpoint.[16] In addition to this proposed change, the Commission also proposes to allow SEFs to issue a confirmation document or trade evidence record to an intermediary that may be trading on behalf of a counterparty, provided that the SEF "establish and enforce rules to require any intermediary to transmit any such document or record to the counterparty as soon as technologically practicable."[17] The Commission noted that industry practice is that, to the extent that an intermediary acts on behalf of swap participants to facilitate execution on a SEF, the SEF ordinarily would transmit a written confirmation to the intermediary and require the intermediary to forward the confirmation to its customer.

The WMBAA supports these proposed changes to allow SEFs to provide a confirmation document or trade evidence record to counterparties "as soon as technologically practicable" after execution. The proposed rule is a reasonable requirement and represents a more practical approach that can be readily adopted by different types of SEFs. The proposed standard of "as soon as technologically practicable" is widely utilized in existing reporting rules and is appropriate to meet the Commission's goals of providing the swap counterparties with legal certainty in a prompt manner. The WMBAA does not believe that the Commission should require SEFs to issue confirmation documents or trade evidence records within a specified time limit. Post-transaction administrative processes vary between swap types, making it difficult or meaningless to set a uniform time limit across all asset classes. With respect to the proposal to allow SEFs to issue a confirmation document or trade evidence record to an intermediary, which may be trading on behalf of a counterparty and must transmit the documentation or record to the counterparties, the WMBAA notes that this is standard industry practice, as swap intermediaries are regulated by the NFA (or a foreign equivalent) and will have regulatory obligations to provide a confirmation or documentation of transactions to their customers.

(5) § 37.201(c) – SEF Trading Specialists

The Commission is proposing new rules for SEF personnel.[18] Such personnel, or "SEF trading specialists," would be part of the SEF's trading system or platform and would be defined as "any natural person who, acting as an employee (or in a similar capacity) of a swap execution facility, facilitates the trading or execution of swaps transactions (other than in a ministerial or clerical capacity), or who is responsible for direct supervision of such persons."[19] In addition, under the proposal, SEFs must adopt minimum proficiency testing and ethics training requirements designed

[16] *Id.* at 61974.
[17] *Id.*
[18] *Id.* at 61989.
[19] *Id.* at 62097.

to ensure that their specialists have and maintain an adequate level of technical knowledge and understand their ethical responsibilities in customer trading or execution and fostering liquidity formation. The Commission stated that this proposal would enhance professionalism requirements for SEF personnel "that operate as part of a SEF's trading system or platform, e.g., voice-based trading functionalities, by facilitating trading and execution on the facility."[20]

The WMBAA believes the term "SEF trading specialist" is misleading and should be changed to "SEF Execution Specialist." The term "SEF trading specialist" connotes someone making trading decisions, but SEF personnel do no such thing. Rather, their primary role is to take instructions from, and help facilitate the execution of transactions between, counterparties to a swap transaction.

The WMBAA supports the proposed requirement that SEF specialists take and pass a proficiency test, which would evidence that they have the knowledge to fulfill their responsibilities as SEF personnel and that they know the applicable provisions of the Act, the Commission's regulations, and rules governing a SEF. The WMBAA also supports the Commission's allowance of third parties, such as the NFA, to create and administer exams. However, the WMBAA notes that the current swaps proficiency examination that is being developed by the NFA does not have a module specifically covering SEF personnel. The Commission should ensure that the examination includes a module covering SEF personnel and clarify that passing the examination of NFA's modules would meet the requirements of § 37.201(c). In cases where a SEF chooses to outsource the administration of its swaps proficiency requirement and the individual taking the examination is strictly a SEF registered person, the NFA should be authorized to administer the examination on behalf of the SEF rather than the SEF offering the examination as an SRO.

(6) § 37.202(a)(2); § 37.3(b)(1) – Access Requirements: Fees; Form SEF: Exhibit K

Existing § 37.202(a)(3) requires a SEF to have a comparable fee structure for eligible contract participants ("ECPs") and independent software vendors ("ISVs") receiving comparable access to, or services from, the SEF.[21] The Commission clarified in a later rulemaking that this requirement neither sets nor limits fees that a SEF may charge and further stated that a SEF may establish different categories of ECPs and ISVs seeking access to, or services from, the SEF, but may not discriminate with respect to fees within a particular category. The Commission also stated that the existing provision was not intended to be a rigid requirement "that fails to take into account legitimate business justifications for offering different fees to different categories of entities seeking access to the SEF."[22]

The Commission is proposing to eliminate the requirement that a SEF must establish comparable fee structures for ECPs and ISVs receiving comparable access to the SEF or services from the SEF. Under proposed rules in § 37.202, a SEF would be allowed to exercise discretion in structuring its participation criteria and trading practices, including fee schedules, as long as the SEF establishes

[20] *Id.* at 61982.
[21] *Id.* 61993.
[22] *Id.*

and applies such fee structures and practices in a "fair and non-discriminatory" manner, which means that such criteria should be non-arbitrary and based on objective, pre-established requirements or limitations.[23] The Commission stated that it is proposing to allow SEFs and market participants the flexibility to determine fees based on legitimate business negotiations, and that the Commission "does not intend to limit the scope of business-related factors that a SEF may continue to consider in establishing participation fee arrangements."[24] According to the Commission, these amendments are intended to provide market participants and SEFs "with the flexibility to negotiate fee arrangements on an individualized basis based on legitimate business justifications."[25]

Given these revisions, the Commission also is proposing to adopt several changes to existing Exhibit K (proposed Exhibit H). The Commission proposes to amend paragraph (a) to require applicants to identify any market maker programs, other incentive programs, or "other discounts on dues, fees, or other charges to be imposed."[26] It further proposes to eliminate the requirement for a description of fee differentials under paragraph (c).

The WMBAA supports the Commission's proposal, but seeks additional clarification on what must be disclosed on Exhibit H. The Commission correctly notes that SEFs have established different fee levels for different categories of market participants or different types of trading activity, where the fees are based on legitimate business considerations and negotiations.[27] The "confluence of factors" has been difficult to distill into fee structures applicable to categories of market participants. The proposed rule changes thus would give SEFs and market participants the flexibility to determine fees based on legitimate business arrangements.

The WMBAA supports the requirement for fair and non-discriminatory (non-preferential) treatment of each participant on a SEF based on its activity and behavioral characteristics. However, it is unclear what information must be disclosed on existing Exhibit K (proposed Exhibit H). Must the fees or charges associated with every individual negotiation be disclosed, or may a SEF disclose on Exhibit K a range of fees within a specified category such that the SEF's negotiated fees with a particular entity would fall within that range without disclosing the specific fee for that transaction? The WMBAA advocates for allowing SEFs to have individual rate agreements that are consistent across similarly situated participants. Requiring SEFs to file individual fee schedules would hinder SEFs' flexibility in the determination of fees associated with these agreements, which across all asset classes can contain hundreds if not thousands of data points.

Rather, the WMBAA recommends that the Commission require SEFs to document all fees in place for all products with all clients and to maintain such documentation. CFTC staff, as part of a periodic examination, could request that the SEF explain and justify why a specific rate (or rates) were established for a specific client(s). Under this approach, Commission staff could assess if there is any discriminatory practice in terms of the setting of fees among clients, while preserving a SEF's

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[23] *Id.* at 61995.
[24] *Id.* at 61997.
[25] *Id.*
[26] *Id.* at 61966. *See also id.* at 62116 (Form SEF: Exhibit K).
[27] *Id.* at 61996-97.

flexibility of negotiation on a client-by-client basis without undue concern as to how fees would be represented in a public schedule that could be requested by a potential participant at any time. This approach would also relieve the Commission from having to review continually changing individual fee schedules and assessing hundreds or thousands of constantly changing data points for each SEF.

(7) § 37.203(e) – Trade Error Policy

Section 37.203(e) currently requires a SEF to conduct real-time market monitoring of all trading activity on its facility and further requires a SEF to have the authority to adjust prices and cancel trades when needed to mitigate "market disrupting events" caused by SEF trading system or platform malfunctions or errors in orders submitted by market participants.[28] Any adjustments or cancellations must be transparent to the market and subject to standards that are clear, fair, and publicly available. In 2013, Commission staff issued guidance ("2013 Staff STP Guidance") to address straight-through processing and expressed the view that SEFs should have rules stating that trades that are rejected from clearing are "void *ab initio*"; that is, that swap transactions rejected by the derivatives clearing organization ("DCO") from clearing would be considered void, even where the rejection is attributable to an operational or clerical error from the SEF or market participants.[29]

After hearing from SEFs that apply the concept of void *ab initio* and their concerns that the requirement has inhibited the ability to correct errors through subsequent trades, Commission staff issued time-limited, no-action relief.[30] Under this relief, SEFs can allow market participants to prearrange corrective trades for execution and submission to a DCO for clearing through means not prescribed for Required Transactions.[31] These trades include a new trade with the corrected terms, where an error trade has been rejected from clearing, and a new trade to offset an error trade accepted for clearing and a second subsequent trade with the corrected terms, as originally intended between the counterparties. However, under the relief, SEFs must still adopt mechanisms to identify these corrective trades and additional, related rules and procedures for their respective market participants. These market participants have stated that those rules and procedures are applied inconsistently, particularly across SEFs. They have recommended the Commission adopt general trade policy requirements to promote a more consistent approach.

The Commission is now proposing to allow a SEF to establish its own rules regarding error trades rejected from clearing for non-credit related reasons,[32] either with respect to a swap rejected by a DCO due to an operational or clerical error or a swap accepted for clearing by a DCO that contains an operational or clerical error. If adopted, the proposal would render unnecessary the current no-action relief.[33] The proposal also would set forth general requirements intended to create a baseline

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[28] *Id.* at 61999.

[29] *Id.*

[30] *Id.* at 62000. This relief has been most recently extended by CFTC Letter No. 17–27, Re: No-Action Relief for Swap Execution Facilities and Designated Contract Markets in Connection with Swaps with Operational or Clerical Errors Executed on a Swap Execution Facility or Designated Contract Market (May 30, 2017).

[31] Required Transactions are those swaps subject to the trade execution requirement.

[32] Under the proposal, SEFs would now be required to deem any swap submitted for clearing as void *ab initio* if a DCO rejects the trade from clearing due to credit reasons. *Proposed Rule*, *supra* note 2, at 62001.

[33] *Id.*

consistency among SEF error trade policies. Among other requirements, a SEF would be required to notify all of its market participants, "as soon as practicable," of any swap transaction that is under review pursuant to the SEF's error trade rules and procedures. In addition, the Commission proposes to define an error trade as "any swap transaction executed on a SEF that contains an error in any term, including price, size, or direction."[34]

The WMBAA supports this proposal, but seeks clarification as to whom the error gets reported when it is discovered. We agree with the Commission's belief the SEFs should have reasonable discretion to determine their error trade policies. However, additional clarification is needed on where responsibility falls when an error is discovered. To whom should the error be reported and when should the error be reported to a swap data repository ("SDR")?

(8) § 37.205 – Audit Trail

Recognizing that technology and practical limitations have impacted SEFs' ability to comply with the current audit trail requirements, the Commission is proposing a number of amendments to simplify and streamline them.[35] In particular, the Commission would clarify existing language in § 37.205(a) to more accurately reflect the capabilities for which a SEF may use its audit trail data and eliminate the requirement that a SEF capture post-execution allocation information.[36] The Commission understands that SEFs are routinely unable to obtain this information.[37] Accordingly, in lieu of requiring that the audit trail track a customer order through "fill, allocation, or other disposition," the Commission proposes to require SEFs to capture the audit trail data only through execution on the SEF.[38]

The Commission also would eliminate the existing audit trail enforcement requirements under § 37.205(c) and adopt an audit trail reconstruction requirement instead.[39] In so doing, rather than dictating specific components of an audit trail not relevant to SEFs, the Commission would allow a SEF to establish its own program. Nonetheless, to still ensure a SEF's audit trail is accurate and sufficient, the Commission would move its current regulatory requirements to guidance at Core Principle 2 in Appendix B.

The WMBAA supports the Commission's proposal regarding audit trail requirements. The current audit trail requirements serve a limited purpose, as their components are either not relevant or not available to SEFs. SEFs cannot and should not be responsible for collecting trade allocation information when the allocations occur away from the SEF. The proposed changes more accurately reflect the capabilities of SEFs to capture audit trail data. The WMBAA does not believe that the proposed rules will lead to degradation of the ability to reconstruct a trade and the environment in

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[34] *Id.*
[35] *Id.* at 62004-07.
[36] *Id.* at 62005.
[37] *See* CFTC Letter No. 17–54, Re: No-Action Relief for Swap Execution Facilities from Certain Audit Trail Requirements in Commission Regulation 37.205 Related to Post-Execution Allocation Information at 2 (Oct. 31, 2017).
[38] *Proposed Rule*, *supra* note 2, at 62005.
[39] *Id.* at 62007.

which it traded. Moreover, the proposed rules will provide more cost-effective alternatives to the current, strict regulatory requirements. Finally, with respect to records of voice bids and offers, the WMBAA supports the requirement that only *executed* voice trades should be part of the surveillance program, but those records should not be part of a SEF's T+1 automated surveillance program as they would be maintained solely for reconstruction of activity in connection with investigations.

(9) § 37.206 – Disciplinary Procedures and Sanctions

Section 37.206 requires a SEF to establish rules that deter abuses and to have the capacity to enforce those rules though prompt and effective disciplinary action.[40] These disciplinary rules further require a SEF to maintain sufficient enforcement staff, establish disciplinary panels, follow certain disciplinary procedures, and impose sanctions that are commensurate to the violations committed. The rules identify different sanctions, including suspension or expulsion of members or market participants, customer restitution, and issuance of warning letters.

The Commission proposes to amend its guidance in Appendix B related to § 37.206(a) by eliminating the language stating that a SEF's enforcement staff may operate as part of the SEF's compliance staff because the Commission "no longer believes this language is necessary, given that SEFs should have the option to determine the appropriate structure for their disciplinary programs."[41]

The Commission also proposes to amend § 37.206(b) to permit a SEF to administer its disciplinary program through not only one or more disciplinary panels, as currently allowed, but also through its compliance staff. The Commission stated that this revision would provide SEFs with "the ability to adopt a cost-effective disciplinary structure that best suits their markets and market participants."[42]

Existing § 37.206(c) requires a SEF to adopt rules that provide minimum procedural safeguards for any hearing, including a fair hearing, promptly convened after reasonable notice to the respondent, and a copy of the hearing to be made and be a part of the record of the proceeding if the respondent requested the hearing.[43] The Commission proposes to eliminate this rule because, among other reasons, it believes that these detailed hearing procedures are not necessary, as SEFs that choose to establish a disciplinary panel have reasonable discretion under Core Principle 1.

Current § 37.206(d) requires a disciplinary panel to render a written decision promptly after a hearing and provides detailed items to be included in the decision.[44] The Commission is proposing to eliminate the requirements in § 37.206(d) because it would be consistent with other proposed amendments to § 37.206 that would allow a SEF to exercise discretion in establishing its disciplinary procedures pursuant to Core Principle 2.

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[40] *Id.* at 62007-08.
[41] *Id.*
[42] *Id.*
[43] *Id.* at 62009.
[44] *Id.*

Existing § 37.206(e) provides that disciplinary sanctions must be commensurate with the violations committed and be sufficient to deter recidivism or similar violation.[45] A SEF also is required to consider a respondent's disciplinary history when evaluating appropriate sanctions. In the event of customer harm, any disciplinary sanction must include full customer restitution where possible. The Commission proposes to consolidate the requirements applying to disciplinary sanctions and warning letters into a new proposed § 37.206(c). The Commission proposes to expand the current use of warning letters by allowing a SEF to issue more than one warning letter over a rolling twelve-month period for violations that involve minor recordkeeping or reporting infractions. These proposals are consistent with "the Commission's goal to provide SEFs with a greater ability to develop cost-effective approaches to administer their disciplinary programs based on their markets and market participants."[46] In addition, the Commission proposes to extend the existing criteria for issuing disciplinary sanctions to warning letters such that all warning letters and sanctions imposed by a SEF must be commensurate with the violations committed and shall be clearly sufficient to deter recidivism or similar violations by other market participants. Further, all warning letters and sanctions, including summary fines and sanctions imposed pursuant to an accepted settlement offer, must take into account the respondent's disciplinary history.

Finally, current § 37.206(f) states that where a rule violation is found to have occurred, no more than one warning letter may be issued per rolling twelve-month period for the same violation.[47] The Commission proposes to amend this provision such that a SEF would be allowed to issue more than one warning letter over a rolling twelve-month period for violations that involve minor recordkeeping or reporting infractions. The Commission stated that it believes that SEFs should have the ability to determine whether infractions warrant a warning letter or sanction. The Commission also proposes to clarify that the twelve-month limitation on warning letters applies to the same individual who is found to have committed the same rule violation, rather than an entity. Further, the Commission notes that the rolling twelve-month period begins tolling once the SEF finds that a violation occurred, rather than the date that the subject activity occurred. Finally, the Commission proposes to eliminate the current guidance to Core Principle 2 in Appendix B that specifies that a SEF may adopt summary fines for violations of rules related to the failure to timely submit accurate records because revised § 37.206(c)(1) already specifies that a SEF may issue summary fines as a sanction.

The WMBAA supports these proposals as they relate to a SEF's disciplinary program. By allowing a SEF to administer its disciplinary program through its compliance staff, a SEF can establish a cost-effective program that meets market participants' demands and still maintains the protections set forth in Core Principle 2. With respect to the question as to whether the Commission should provide further explanation regarding the meaning of "minor" recordkeeping or reporting infractions, the WMBAA believes that further, descriptive meaning of "minor recordkeeping or reporting infractions" would be inconsistent with providing a SEF with the ability to create disciplinary and operational rules specific to the operating circumstances of the individual SEF.

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[45] *Id.*
[46] *Id.*
[47] *Id.* at 62010.

(10) §§ 37.301; 37.402 – General Requirements & Additional Requirements for Physical-Delivery Swaps (Monitor Physical Settlement)

Core Principle 3 specifies that a SEF shall permit trading only in swaps that are not readily susceptible to manipulation. The Commission proposes to eliminate the existing cross-reference to Appendix C to part 38 under § 37.301 and establish a separate Appendix C to part 37 to provide specific guidance to SEFs for complying with the requirements of Core Principle 3.[48] In conjunction with the Commission's proposal to create a separate Appendix C to part 37, the Commission also proposes to adopt conforming changes to the guidance to Core Principle 3 in Appendix B.

Core Principle 4 requires a SEF to establish and enforce rules that define, or specifications that detail, the trading procedures used in entering and executing orders traded on or through the facilities of the SEF and procedures for trade processing of swaps on or through the facilities of the SEF.[49] Core Principle 4 also requires a SEF to monitor trading in swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement process through surveillance, compliance, and disciplinary practices and procedures. As part of its monitoring responsibilities, a SEF must establish methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.

The Commission received feedback from SEFs that certain requirements are unnecessarily broad and create impracticable monitoring burdens upon SEFs. Based on its experience, the Commission proposes amendments that would establish more practical monitoring requirements.[50] These amendments narrow a SEF's monitoring obligations to trading activity on its own facility and allow a SEF greater discretion to devise its own monitoring systems and protocols.

Section 37.401 currently implements Core Principle 4 by setting forth requirements for SEFs to monitor market activity for the purpose of detecting manipulation, price distortions, and disruptions.[51] Existing § 37.401(a) creates an ongoing obligation for a SEF to collect and evaluate data on its market participants' market activity to detect and prevent, among other things, disruptions to the physical-delivery or cash-settlement process where possible. Existing § 37.401(b) requires a SEF to examine general market data in order to detect and prevent manipulative activity that would result in the failure of market prices to reflect the normal forces of supply and demand. Existing § 37.401(c) requires a SEF to demonstrate an effective program for conducting real-time monitoring of trading for the purpose of detecting and resolving abnormalities.

For swaps settled by physical delivery, § 37.402 requires that a SEF monitor each swap's terms and conditions as they relate to the underlying commodity market and monitor the "availability of supply" of the underlying commodity, as specified by the swap's delivery requirements.[52] The Commission provided guidance that a SEF should monitor the general "availability" of the

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[48] *Id.* at 62011.
[49] *Id.* at 62012.
[50] *Id.*
[51] *Id.*
[52] *Id.* at 62014.

commodity specified by the swap; the commodity's characteristics; the delivery locations; and if available, information related to the size and ownership of deliverable supplies. The Commission proposes to clarify a SEF's monitoring obligations with respect to physical-delivery swaps to be consistent with the guidance in proposed Appendix C to part 37 and ensure that the SEF can comply with Core Principles 3 and 4. Among other things, a swap contract's terms and conditions should assure the availability of adequate deliverable supplies, such that the contract is not readily susceptible to price manipulation.

Revised § 37.402 would require a SEF to (i) monitor the swap's terms and conditions as they relate to the underlying commodity market by reviewing the convergence between the swap's price and the price of the underlying commodity, and make a good-faith effort to resolve conditions that are interfering with convergence or notify the Commission of such conditions; and (ii) monitor the availability of the supply of the commodity specified by the delivery requirements of the swap, and make a good-faith effort to resolve conditions that threaten the adequacy of supplies or the delivery process or notify the Commission of such conditions.

The Commission notes that Core Principles 3 and 4 place affirmative obligations on SEFs to permit trading only in swaps that are not readily susceptible to manipulation and prevent manipulation, price distortion, and disruptions of the delivery or cash-settlement process, respectively. As such, proposed § 37.402 places affirmative obligations on a SEF to make a good-faith effort to resolve conditions that are interfering with convergence or that threaten the adequacy of supplies or the delivery process. The Commission recognizes, however, that a SEF may not always be able to resolve these conditions; therefore, proposed § 37.402 allows the SEF to notify the Commission of such conditions.

The Commission further proposes corresponding amendments to the associated guidance to Core Principle in Appendix B.[53] The Commission proposes a non-substantive revision to clarify that a SEF should monitor physical-delivery swaps listed on its facility. To conform to Core Principle 4, the Commission also proposes to clarify that a SEF should monitor for conditions that may cause a swap to become susceptible to manipulation, price distortion, or disruptions; such conditions would include those that influence the convergence between the swap's price and the price of the underlying commodity. This proposed language would conform to the proposed guidance for physically-settled swaps in the proposed Appendix C to part 37, which states that a physically-settled swap contract's terms and conditions should be designed to avoid any impediments to the delivery of the commodity so as to promote convergence between the value of the swap contract and the cash market value of the commodity at the expiration of the swap contract.

The Commission also proposes a non-substantive change to eliminate the demonstration-based requirement under § 37.402. As noted above, the Commission proposes to set forth an affirmative monitoring requirement for SEFs, rather than a demonstration requirement. The Commission notes that demonstration of compliance could otherwise be required upon Commission request under

[53] *Id.* at 62015.

§37.5(b), which requires a SEF to provide a written demonstration that it is in compliance with its obligations under the Commodity Exchange Act.

The WMBAA generally supports the proposed changes to §37.402 and the Commission's proposal to clarify a SEF's monitoring obligations with respect to physical-delivery swaps under § 37.402 to be consistent with the guidance in proposed Appendix C to part 37 and ensure that the SEF can comply with Core Principles 3 and 4. The WMBAA appreciates the Commission's recognition that a SEF has limited ability to monitor activity in physical commodities beyond activity on its own markets. It is impractical for a SEF to monitor underlying general "availability" of a commodity specified by a swap, delivery locations, and information related to the size and ownership of deliverable supplies.

The WMBAA supports the Commission's more realistic and practical method for a SEF to monitor for conditions under the proposed changes to §37.402. The WMBAA appreciates the Commission's recognition that a SEF may not be able to resolve unusual or disruptive deliverable supply or underlying pricing conditions and, therefore, proposes in § 37.402 to allow a SEF to notify the Commission of such conditions.

While these realizations are more reflective of reality for an execution facility such as a SEF, which does not own, clear, or settle the swaps that are traded on their facility, the WMBAA notes that the "price convergence at expiration/delivery" concept appears based on and more appropriate to the futures market rather than the swap market. Most swap contracts (physically or financially settled) are traded with rolling expiration, settlement, or maturity dates set at intervals from the swap start date (e.g., 1-month, 2-months, 1-year, 2-years, etc.). This convention reflects the customary hedging practices of their underlying markets. The result is that swaps mature, expire, or settle every day, unlike futures contracts, which settle on fixed dates in a cycle (e.g., fixed dates in March, June, September, and December), where a concentration of positions may be more likely to have an influence on price or deliverable supply. When promulgating rules for monitoring trading and settlement activity, the WMBAA would appreciate the Commission's consideration of the daily rolling settlement nature of swaps, as well as the operational reality that settlement of physically settled swaps occurs away from the control and view of SEFs, as factors which further mitigate the risk of swap delivery affecting prices or physical supply.

Additionally, the WMBAA requests the Commission consider a more specific distinction between swaps that settle in physical commodities, such as natural resources or agricultural commodities, and other swaps that settle in financial instruments, such as currencies, with respect to monitoring supply and market conditions of physically settled swaps. WMBAA SEFs generally offer physically settled swaps and options that settle into an underlying currency or financial instruments, where central banks or monetary authorities manage a nation's currency. In each of these instances, SEFs should be able to generally rely upon central banks or monetary authorities to monitor and prevent manipulation of their respective currencies, as such institutions are statutorily mandated with managing their country's currency and such management is a sovereign right of a country issuing a currency. Further, it is highly unlikely that a market participant might assert control, or attempt to assert control, over the supply of a currency or financial instrument through an individual SEF.

(11) § 37.403 – Additional Requirements for Cash-Settled Swaps

The Commission has acknowledged that the requirement imposed by §37.403(a) to monitor the methodologies behind third-party indexes or instruments is not realistic due to the proprietary nature of these indexes and instruments.[54] The Commission has observed that many SEFs offer swaps for which pricing is based on benchmark prices or benchmark indices owned or administered by third parties, and that requiring a SEF to monitor the inputs and calculations involved in those methodologies on an ongoing basis is impractical, especially when considering that certain aspects of the benchmarks are proprietary. Therefore, the Commission acknowledged that SEFs do not necessarily have full access to the information to monitor trading to detect disruptions or manipulations of indexes or reference rates administered by other industry participants.

Based on these considerations, the Commission is proposing to eliminate the requirement that SEFs monitor the "pricing" of the reference price used to determine cash flows or settlement. Where the reference price relies on a third-party index or instrument, a SEF would continue to be required to monitor the "appropriateness" of the index or instrument; the Commission, however, proposes to amend this requirement to additionally require a SEF to take appropriate action, including selecting an alternate index or instrument for deriving the reference price, where there is a threat of manipulation, price distortion, or market disruption. The Commission believes that sufficient information is generally available to SEFs to comply with this proposed requirement and expects that a SEF would take action with respect to its use of a third-party index or instrument for a listed swap contract that would inhibit the SEF's ability to prevent manipulation pursuant to Core Principles 3 and 4.

The WMBAA previously commented on the impracticality of certain aspects of § 37.403.[55] The WMBAA explained that it would be impossible or impractical for a SEF to obtain the information to appropriately monitor the availability, pricing, and methodology for the index from third-party index providers, which make up the vast majority of indexes underlying cash-settled swaps. The WMBAA said:

> This requirement is likely to be impossible for SEF compliance. In the present swaps marketplace, intermediaries do not necessarily execute transactions in the underlying instruments or commodities that serve as reference information for the respective swaps. As such, a SEF will most likely lack access to the necessary reference information underlying an index to appropriately monitor the availability, pricing, and methodology for the index.

The WMBAA also commented that "[t]his burden is more appropriately borne by those setting the index or a third party with necessary access to the information and the capabilities to analyze the data. Alternatively, this requirement might be carried out by a third party service provider who is

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[54] *Id.*

[55] *See* Letter from WMBAA to David Stawick, Secretary, CFTC regarding Core Principles and Other Requirements for Swap Execution Facilities (RIN 3038–AD18) (March 8, 2011).

able to collect information related to SEF trading activity and the underlying commodities making up an index in order to meet the monitoring requirements of the Proposed Rules."

The WMBAA supports the proposed changes to § 37.403 and the elimination of the associated guidance to Core Principle 4 in Appendix B. The WMBAA appreciates the Commission's recognition of the impracticality of a SEF's ability to monitor the methodologies behind third-party indexes or instruments due to the proprietary nature of these indexes and instruments. The WMBAA agrees that where a swap reference price relies on a third-party index or instrument, a SEF should be able to monitor the appropriateness and commercial acceptability of the index or instrument, and take appropriate action, including selecting an alternate index or instrument for deriving the reference price, where the SEF considers there to be a threat of manipulation, price distortion, or market disruption to a reference price.

(12) § 37.601 - Additional Sources for Compliance; Guidance to Core Principle 6 in Appendix B

Core Principle 6 requires a SEF to adopt, as is necessary and appropriate, position limits or position accountability levels for each swap contract.[56] For contracts that are subject to a federal position limit, the SEF must set its position limits at a level that is no higher than the limit established by the Commission; and monitor positions established on or through the SEF for compliance with the Commission's limit. The guidance to Core Principle 6 in Appendix B of Section 37.601 implements Core Principle 6 and specifies that, until such time that compliance is required under part 151 of the Commission's regulations, a SEF may refer to the associated guidance and/or acceptable practices set forth in Appendix B to § 37.6. The Commission stated that it is proposing to eliminate the language of § 37.601 and the existing corresponding guidance to Core Principle 6, based on its intent to address this issue in a separate rulemaking. Until that time, the Commission clarifies that SEFs have reasonable discretion to determine how to comply with Core Principle 6.[57]

The WMBAA has commented on position limits and accountability on multiple occasions since the first publication of proposed SEF Rules by the CFTC in 2011. While the WMBAA understands and agrees with the public policy and market purposes with respect to position limits in the swaps and futures markets, the WMBAA's position remains unchanged. SEFs do not possess information about a participant's position in any given swap or its underlying instrument or commodity. Rather, SEFs only have information about the economic terms of swap transactions that take place on their individual facilities and have no way of knowing whether a particular trade on their facility adds to an existing market-wide position or whether it offsets all or part of an existing position in that swap.[58] Absent statutory revision to reflect the nature of a SEFs role as merely a facilitator of liquidity in the swaps market, the WMBAA suggests (1) removing the impractical burden for

[56] *Proposed Rule*, *supra* note 2, at 62018.
[57] *Id.* at 62019.
[58] Thus, the enforcement of position limits by individual SEFs is impossible. SEFs are execution facilities that do not possess the requisite market information to monitor position limits and do not have the legal or commercial control over positions held by their participants. Moreover, each SEF lacks knowledge of a market participant's activity on other venues which precludes it from being able to calculate a position of a market participant.

establishing and ensuring compliance with swaps position or accountability limits from SEFs and (2) mandating that position limits be established by the CFTC and monitored for compliance by either the CFTC or a designated regulatory authority. In either case, the entity would have full access to the positions in swaps and related instruments, which would facilitate effective oversight of swap participant's overall positions. Further, the WMBAA urges the CFTC to encompass the revisions in its future separate rulemaking with respect to Core Principle 6 into its final Part 37 rules.

In sum, the WMBAA believes that a position limits regime is one of many areas in which the Commission or a third-party regulatory service provider might have access to the information necessary to effectively adopt, monitor, and enforce swap position limits. Such information is not available to a SEF.

(13) § 37.801 – Emergency Authority: Additional Sources for Compliance

Core Principle 8 requires a SEF to adopt rules to provide for the exercise of emergency authority, in consultation or cooperation with the Commission, as is necessary and appropriate, including the authority to liquidate or transfer open positions in any swap or to suspend or curtail trading in a swap.[59] The current guidance to this core principle in Appendix B specifies, among other things, the types of emergency actions that a SEF should take in particular to address perceived market threats, and states that the SEF should promptly notify the Commission of its exercise of emergency action.

The Commission proposes in § 37.801 to eliminate references to certain emergency actions that a SEF, as a matter of general market practice, would not be able to adopt, including imposing special margin requirements and transferring customer contracts and the margin.[60]

The WMBAA strongly supports these revisions to the Core Principle 8 guidance. Since SEFs do not own the contracts, they do not have the ability to impose margin requirements or transfer contracts. The WMBAA further notes that the revised guidance states: "[t]o address perceived market threats, the swap execution facility should have rules that allow it to take emergency actions, including imposing or modifying position limits . . . ."[61] The Commission, in its final rules, should remove any reference to position limits as a course of action available to a SEF in dealing with an emergency. As the WMBAA has previously stated, SEFs do not possess information about a trader's position in any given swap or its underlying instrument or commodity and do not have the means to enforce position limits. SEFs only have information about swap transactions that take place on their individual facilities and have no way of knowing whether a particular trade on the facility adds to an existing market-wide position or whether it offsets all or part of an existing position in that swap.

(14) § 37.1301 – Core Principle 13 (Financial Resources) – General Requirements

Core Principle 13 requires a SEF to have adequate financial, operational, and managerial resources to discharge each of its responsibilities. After receiving feedback from SEFs, including from the

[59] *Id.* at 62024.
[60] *Id.*
[61] *Id.* at 62134.

WMBAA, that the existing requirements impose impractical financial and operating burdens, the Commission is now proposing several amendments to "achieve a better balance between ensuring SEF financial stability, promoting SEF growth and innovation, and reducing unnecessary costs."[62]

The WMBAA supports the Commission's proposed revisions to Core Principle 13. The WMBAA commends the Commission's recognition that SEFs are fundamentally different than designated contract markets ("DCMs"), upon which the current SEF financial requirements were modeled. SEFs are execution platforms for universally accepted swap contracts. They do not own or clear the contracts that are traded on their platforms, nor do they possess or maintain client funds or open interest. There is no practical need for any individual SEF to maintain sufficient resources for a period of one-year after an event that results in the closure of a SEF, as a SEF could wind down its operations in a much shorter time period and its participants could transfer their trading to a competing SEF. Furthermore, for SEFs with voice brokers, such voice brokers are not necessary to ensure operation of a compliant SEF and could be removed at any point and for any reason without impacting the SEF's ability to satisfy the Core Principles. The WMBAA does not believe that the proposed reduction in financial requirements would impair a SEF's stability or the swap marketplace for the reasons stated above. The proposed changes should encourage innovation and new entrants into the marketplace as the cost of entry should be lower than at present. Further to the discussion of general requirements for SEF financial resources, the WMBAA urges the Commission to support allowing dual-hatted SEF voice brokers and allocation of their costs, which is beneficial for financial resource calculation, and requests that the Commission allow other regulated entities, such as broker dealers, to own a SEF, which might be capital efficient for both regulated entities. The WMBAA also supports allowing the use of credit facilities for the financial resource calculation

(15) § 37.1303 Liquidity of Financial Resources

For the reasons summarized in the WMBAA's comments regarding § 37.1301 above, the WMBAA is requesting that the CFTC allow SEFs to include all commissions receivable aged less than three months ("liquid receivables") as liquid assets, and, therefore, permitted to be included in a SEF's liquid financial resource requirement calculation. Permitting the use of liquid receivables would not impair a SEF's ability to perform its core functions; rather, it would enable a SEF to avoid locking up/trapping cash unnecessarily, which may result in a SEF investing in growth or innovation that might not be economical under the current liquidity requirement. The collection of commissions receivable typically average between 30 and 90 days; therefore, the turnover/conversion to cash would be executed easily and timely, thus providing cash available to cover a SEF's projected three months operating costs and/or wind down costs. The WMBAA also urges the Commission to allow revolving subordinated debt as a liquid asset in the financial resource requirement.

The WMBAA also suggests allowing a six-month grace period from the effective date of the revised rules to the application of the new financial resource requirements. This would give SEFs time to build capital in the form of retained profits from products transferred into the SEF from its

[62] *Id.* at 62025.

introducing broker entities along with the associated costs of those brokers and alleviate the potential burden associated with substantial capitalization/recapitalizations associated with the startup period. This may not eliminate the need for interim capitalization, but would at the very least remove excess capitalization required during the ramp-up period.

(16) § 37.1304 – Computation of Costs to Meet Financial Resources Requirement

To help SEFs comply with Core Principle 13, the Commission is proposing acceptable practices that, among other things, would permit a SEF to include only the costs related to one of the "bona fide" execution methods that it offers.[63]

The WMBAA supports the acceptable practices recommended by the Commission. However, the Commission needs to provide clarity on what a "bona fide" execution method means, so that a SEF knows how to calculate its financial requirements. The WMBAA believes that, with the expanded scope of trades that will be required to be executed on a SEF, many of the products will have limited liquidity. The fact that a product may have limited to no regular interest should not render an execution methodology to be considered non-bona fide. Many SEFs provide fully electronic central limit order books ("CLOBs"); however, this does not mean clients will post bids or offers to the CLOB. Because many swaps are bespoke, a SEF may not list each variation of a swap in its CLOB. However, this should not limit the SEF in considering its CLOB as a bona fide execution method in calculating its financial requirements.

(17) §37.1306(a) – Reporting to the Commission

Section 37.1306 establishes a SEF's financial reporting requirements to the Commission. In particular, subsection (a) requires that, at the end of each fiscal quarter or upon Commission request, a SEF must report to the Commission (i) the amount of financial resources necessary to meet the financial resources requirement; and (ii) the value of each financial resource available to meet those requirements. The Commission is proposing, among other changes to this subsection, that a SEF be required to prepare its financial statement in accordance with generally accepted accounting principles in the United States ("GAAP"). The Commission asks whether these reports also should be required to be audited.

The WMBAA does not believe the SEF's financial reports should be required to be audited. There are a number of variables used to determine and calculate a SEF's financial resources (e.g., bona fide execution methodologies and forward projections of costs based on historical or estimated costs) on which an auditing firm would be unlikely or unwilling to opine. Moreover, audited financials would likely not improve any Commission oversight. The Commission has the authority to audit SEFs. The costs for annual audits would be significant, and an annual audit requirement would act as a barrier for new entrants or novel, limited scope platforms

The WMBAA believes the current requirement to submit four financial reports is sufficient to ensure capital adequacy. In fact, given the nature of a SEF, the WMBAA believes that a semi-annual

[63] *Id.* at 62028.

and annual report would be adequate. As part of moving to a semi-annual and annual reporting requirement, a SEF should be required to maintain all documentation and support related to any reports filed with Commission for additional inspection. For intra periods, the SEF should not be required to prepare and maintain all of the supplemental reporting and related support. Rather, it should be required to maintain a calculation showing balance sheet and required financial resource and liquidity calculations based on the requirement identified in the most recent filing to the Commission. SEF financial statements should be prepared in accordance with U.S. GAAP or its equivalent (e.g., International Financial Reporting Standards ("IFRS")) for those entities outside of the United States. This would provide some comparability among reported amounts by SEFs from various regions.

(18) § 37.1501 – Designation of Chief Compliance Officer and Submission of Annual Compliance Report

(a) § 37.1501(a) – Definition of Senior Officer

Core Principle 15 requires each SEF to designate a chief compliance officer ("CCO") and sets forth the CCO's responsibilities, including ensuring that the SEF complies with applicable rules and regulations, establishes and administers policies and procedures, and prepares and files an annual compliance report ("ACR") to the Commission.[64] The Commission stated that, based on its experience, it is proposing a number of amendments to § 37.1501 to streamline the requirements related to the ACR and provide more useful information to the Commission.

First, Core Principle 15 requires a CCO to report directly to the SEF's "board [of directors]" or the SEF's "senior officer." While board of directors is defined in the rule, senior officer is not. The Commission is now proposing to define senior officer in amended § 37.1501(a) as "the chief executive officer or other equivalent officer of the SEF."[65] The Commission stated that it has noted that such a senior officer may be the appropriate individual to whom a CCO would report regarding SEF activities; thus, the proposal would "clarify the permissible reporting lines for the CCO and would provide specificity to the Commission's proposed amendments to the Core Principle 15 regulations . . . ."[66]

The WMBAA supports the proposed amendments to add a definition of senior officer. The revised rules should eliminate duplicative or unnecessary requirements, streamline existing provisions, and thereby allow SEFs to meet their statutory and regulatory obligations in a more effectively and less burdensome manner.

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[64] *Proposed Rule*, *supra* note 2, at 62032.
[65] *Id.*
[66] *Id.*

(b) § 37.1501(b) – CCO Position Requirements

Sections 37.1501(b)–(c) set forth various requirements for the SEF CCO position, including, among other things, that the CCO have the authority and resources to meet its duties and supervisory responsibilities over compliance staff; the SEF establish qualifications for the CCO; and the CCO meet with the SEF board and regulatory oversight committee on a regular basis.[67]

The Commission is proposing to consolidate certain provisions in the rules and eliminate duplicative rules. It also is proposing to allow a SEF's senior officer to have the same oversight responsibilities over the CCO as the board of directors by allowing the CCO to consult with the board of directors or senior officer in developing policies and procedures, meet with the senior officer of the SEF, in addition to the board of directors, and allow the CCO to provide self-regulatory program information to the SEF's senior officer, in addition to the board. The Commission further proposes to eliminate the limitations on authority to remove a CCO by adopting a more simplified requirement. The Commission explained that, based on its experience, the senior officer "may be better positioned than the board to provide day-to-day oversight of the SEF and the CCO, as well as to determine whether to remove a CCO."[68] Thus, the Commission stated that a SEF's senior officer should have the same CCO oversight authority as the SEF's board of directors because it would ensure a level of independence for its CCO that is appropriate to comply with Core Principle 15.

Finally, the Commission proposes in Appendix B a new acceptable practice related to the requirement that a CCO have the background and skills appropriate to the position. Specifically, the proposed acceptable practice includes a non-exclusive list of factors that may be considered when evaluating a person's qualifications as a CCO. The Commission stated that the proposed list provides "the clarity that SEFs have sought as to a CCO's requisite qualifications, but still allows a board and senior officer reasonable flexibility in appointing a CCO."[69] The acceptable practice would further provide that the SEF should be vigilant in identifying potential conflicts of interest, as the "Commission continues to believe that conflicts of interest could affect a CCO's ability to effectively fulfill his or her responsibilities."[70]

The WMBAA supports the proposed amendments to the requirements for the CCO position. The revised rules should eliminate duplicative or unnecessary requirements, streamline existing provisions, and thereby allow SEFs to meet their statutory and regulatory obligations in a more effective and less burdensome manner.

(c) § 37.1501(c) – CCO Duties

Existing rules requires a CCO to oversee and review the SEF's compliance with the Commodity Exchange Act ("Act") and regulations, resolve conflicts of interest, establish and administer written policies and procedures reasonably to prevent violations of the Act, take reasonable steps to ensure

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[67] *Id.*
[68] *Id.* at 62033.
[69] *Id.*
[70] *Id.*

compliance with the Act and regulations, establish procedures for the remediation of noncompliance issues, establish procedures for addressing noncompliance issues, administer a compliance manual and a written code of ethics, supervise the SEF's self-regulatory program, and supervise the effectiveness and sufficiency of any regulatory services provided to the SEF.[71]

The Commission proposes to consolidate within the revised rule certain provisions, specify that a CCO may identify noncompliance matters through "any means" in addition to currently specified means, and clarify that the procedures followed to address noncompliance issues must be "reasonably designed."[72] The Commission states that these amendments "acknowledge that a CCO may not be able to design procedures that detect all possible noncompliance issues and reflect that a CCO may utilize a variety of resources to identify noncompliance issues."[73] The Commission also is proposing to modify the CCO's duty to resolve conflicts of interest by limiting a CCO's duty to address only "material" conflicts of interest, because the current requirement is overly broad and impractical such that a CCO cannot reasonably be expected to resolve every potential conflict of interest that may arise. In addition, the Commission proposes to narrow the scope of the CCO's duty to taking only "reasonable steps" to resolve "material" conflicts of interest that may arise and to eliminate the existing list so that they are not interpreted as a comprehensive list of conflicts of interest that a CCO must address. The Commission stated that these amendments "reflect the CCO's practical ability to detect and resolve conflicts" and reflect the Commission's belief that a CCO should have discretion to determine if conflicts are material.[74]

The WMBAA supports the proposed amendments to the CCO's duties. The revised rules should eliminate duplicative or unnecessary requirements, streamline existing provisions, and thereby allow SEFs to meet their statutory and regulatory obligations in a more effective and less burdensome manner.

(d) § 37.1501(d) – Preparation of the Annual Compliance Report

Existing rules requires a CCO to prepare and sign an annual compliance report ("ACR") that (i) describes the SEF's written policies and procedures; (ii) reviews the SEF's compliance with the Act and regulations; (iii) provides a self-assessment of the effectiveness of the SEF's policies and procedures; (iv) lists material changes to the policies and procedures; (v) describes the SEF's financial, managerial, and operational resources; (vi) describes any material compliance matters; and (vii) certifies that, to the best of the CCO's knowledge and reasonable belief and under penalty of law, the ACR report is accurate and complete.[75]

The Commission is proposing amendments to eliminate duplicative or unnecessary requirements, streamline existing requirements, and reduce regulatory burdens and compliance costs. Specifically, under the proposal, SEFs would not need to include in an ACR a review of all the Commission

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[71] *Id.* at 62033-34.
[72] *Id.* at 62034.
[73] *Id.*
[74] *Id.*
[75] *Id.*

regulations applicable to a SEF or an identification of the written policies and procedures designed to ensure compliance, and could instead include a description and self-assessment of the effectiveness of the SEF's policies and procedures. Also, a SEF would no longer need to discuss its compliance staffing and structure, all investigations and disciplinary actions, and a review of disciplinary committee and panel performance, but must instead require the SEF to describe and self-assess the effectiveness of its policies and procedures to "reasonably ensure" compliance with the Act and regulations. The ACR would continue to require a description of the financial, managerial, and operational resources set aside for compliance. The Commission states that these changes would allow SEF's "to devote its resources in providing more detailed, and ultimately better quality, information that will better help assess its compliance."[76] The Commission also proposes to require a SEF to discuss only material noncompliance matters and explain the actions taken to resolve those issues. Finally, the Commission proposes to eliminate the specified mechanisms for identifying noncompliance issues and to limit the CCO's certification of an ACR's accuracy and completeness to "all material respects" of the report.

The WMBAA supports the proposed amendments to the preparation of the ACR. The revised rules should eliminate duplicative or unnecessary requirements, streamline existing provisions, and thereby allow SEFs to meet their statutory and regulatory obligations in a more effectively and less burdensome manner.

(e) § 37.1501(e) – Submission of ACR and Related Matters

Existing rules requires a CCO to submit the ACR to the board of directors or senior officer for review, and the board or senior officer may not require the CCO to change the ACR.[77] The SEF's board minutes or a similar written record must reflect the submission of the ACR to the board of directors or senior officer and any subsequent discussion of the report. The SEF must file the ACR and the fourth quarter financial statements with the Commission within 60 calendar days of the end of the SEF's fiscal year end; however, a SEF may request an extension based on substantial, undue hardship in filing the ACR on time.

The Commission proposes several amendments to refine the scope of some of the ACR's content and procedures it believes is otherwise duplicative, unnecessary, or burdensome. Under the proposal, a SEF would no longer need to include in its ACR either a review of all the Commission regulations applicable to a SEF or an identification of the written policies and procedures designed to ensure compliance with the Act and Commission regulations.[78] The Commission would further codify no-action relief by providing SEF's with an additional 30-days to file the ACR with the Commission, but no later than 90 calendar days after a SEF's fiscal year end, and would replace the "substantial and undue hardship" standard required for filing an extension with a "reasonable and valid" standard.[79] Finally, the Commission proposes to eliminate the requirement that a SEF must

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[76] *Id.* at 62035.
[77] *Id.*
[78] *Id.*
[79] *Id.* at 62036.

document the submission of the ACR to the board or senior officer in board minutes or some other similar written record.

The WMBAA generally supports this proposal to amend the ACR's submission requirements. Amendments that eliminate duplicative or unnecessary requirements will allow SEFs to focus on meeting the Commission's other burdensome and expensive, yet nonetheless necessary, regulatory requirements.

(19) § 43.2 – Definition of "Block Trade"

As defined under § 43.2, a block trade involves a SEF- or DCM-listed swap transaction with a notional or principal amount that is above the appropriate minimum block size established by the Commission for that swap.[80] A swap that a SEF or DCM allows to be executed as a block trade away from a SEF is subject to the time delay requirements in Part 43 and may be privately negotiated to avoid potentially significant and adverse price impacts that would occur if traded on trading systems or platforms with pre-trade price transparency. The Commission's rules, however, require that swap block trades "occur away" from a SEF's or a DCM's trading system or platform, but pursuant to the SEF's or a DCM's rules and procedures.[81] Since this latter requirement created operational challenges for SEFs because they were unable to facilitate pre-execution credit checks for block trades, the Commission granted ongoing no-action relief from the requirement that swap block trades "occur away" from a SEF.[82]

The Commission is proposing to codify the existing no-action relief by eliminating the "occurs away" requirement for swap block trades in §43.2.[83] In addition, the Commission proposes to require that, to the extent counterparties seek to execute any swap that has a notional or principal amount at or above the minimum block trade size, they must do so on the SEF's trading system or platform. The Commission notes that, by eliminating the prescriptive execution methods and allowing more flexible execution for swaps subject to the trade execution requirement, pre-execution communications, including the negotiation or arrangement of block trades, would be able to occur entirely within a SEF's trading system or platform.

The Commission explains that these revisions are consistent with provisions of the Dodd-Frank Act, which directs the Commission to prescribe criteria for determining what constitutes a block trade for the purpose of establishing appropriate post-trade reporting time delays. The Dodd-Frank Act does not establish pre-trade requirements, such as a requirement that a block swap transaction be executed away from a SEF. In addition, the Commission justified the proposed changes by stating that requiring block trades to be executed on a SEF for those swaps listed by the SEF, rather

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[80] *Id.* at 62042-43.

[81] *Id.* at 62043.

[82] *Id. See also* CFTC Letter No. 17–60, Re: Extension of No-Action Relief for Swap Execution Facilities from Certain "Block Trade" Requirements in Commission Regulation 43.2 (Nov. 14, 2017).

[83] *Proposed Rule*, *supra* note 2, at 62043.

than allowing them to be executed away from the SEF would facilitate the statutory goal of promoting swaps trading on SEFs.[84]

The WMBAA strongly supports the Commission's proposal to eliminate the "occurs away" requirement for swap block trades on SEFs. The existing requirement is a carryover from the regulations governing futures markets, has created operational challenges for SEFs as Commission staff has acknowledged, and is contrary to the public policy objective in the context of encouraging swap trading on SEFs. The WMBAA also does not support placing any limits on the types of execution methods that may be utilized by SEFs for block trades. Placing limits on the types of execution methods that are employable for block trades is inconsistent with the statute, which was clear that limiting modes of SEF execution was not the intent of Congress. In so doing, though, the current rules allow block trades and other trades to escape regulated SEF trading. The proposed rules are more consistent with the statute. With respect to the proposal that counterparties seeking to execute block trades with respect to SEF-listed swap must do so on a SEF's trading system or platform, the WMBAA believes that the Commission should defer to the SEFs to determine the methodology that they wish to offer for executing block trades. SEFs have the greatest knowledge of the liquidity and market characteristics to make such determinations. Finally, the WMBAA believes that, consistent with the requirements set forth in section 2(a)(13) of the Act, the Commission should maintain the current process whereby the CFTC, and not individual SEFs, prescribes the levels and criteria for determining what constitutes a block trade for particular markets and contracts and the appropriate time delay for reporting such block trades to the public.

III. ADDITIONAL COMMENTS

In addition to the comments above related to specific proposals in the Proposed Rule, the WMBAA believes that there are several other matters involving swap trading that the Commission should address in promulgating a final rule. These matters include the embargo rule, the recordkeeping retention period, the floor trader exemption, and margin requirements for swaps.

(1) The Embargo Rule

Pursuant to § 43.3(b)(3), commonly referred to as the embargo rule, a SEF may not disclose swap and pricing data with respect to transactions on its facility to market participants until it transmits such data to an SDR for public dissemination.[85] In order to submit such data to the SDR, a SEF must ensure that the data is in the format specified by the SDR or, alternatively, use a third-party provider to transmit the data to the SDR. Only then can the SEF disclose swap transaction data to market participants on its facility. As Chairman Chris Giancarlo articulated in his 2015 White Paper:

> The delays in transaction and pricing data disclosure caused by the embargo rule inhibit the long-established "work-up" process, whereby counterparties buy or sell additional quantities of a swap immediately after its execution on the SEF at a price matching that of the original trade. It is believed that the work-up process increases

[84] *Id.* at 62044.
[85] 17 CFR 43.3(b)(3).

> wholesale trading liquidity in certain OTC swaps by as much as 50 percent. The embargo rule thwarts this liquidity generation. This rule has hindered U.S. markets from continuing a well-established and crucial global trading mechanism. The effect of the embargo rule appears to prioritize public transparency – in a market that is closed to the general public – at the expense of transparency for actual participants in the marketplace. It is difficult to justify this unbalanced restraint on swaps liquidity. [86]

The WMBAA concurs with Chairman Giancarlo's observations and thus recommends that the Commission eliminate the embargo provisions in § 43.3(b)(3). As a result of the embargo rule, SEFs that would like to permit work-ups as a necessary and vital component of the trade execution process face workflow issues because they cannot share trade information with their customers until such information is transmitted to an SDR even though the price of the product does not change during the work-up phase. Such delays can have a material effect on market liquidity. To operate efficiently and competitively, information that reflects current market activity must be available to market participants without any disruptive pauses for the occurrence of other regulatory activities. Market participants must have real-time information on executed trades to ensure effective price discovery, so that they can make informed trading decisions. This allows the market to operate properly as a single liquidity pool. In addition, those SEFs that rely on a third-party to transmit information to SDRs are further hindered by the embargo rule in their ability to make available to all market participants current market information.

(2) The Recordkeeping Retention Period

Section 45.2(c) provides that SEFs, as well as designated contract markets, derivatives clearing organizations, swap dealers, and major swap participants, must retain all records required to be kept pursuant to § 45.2 "throughout the life of the swap and for a period of at least five years following the final termination of the swap."[87] This obligation is an onerous and impracticable requirement for SEFs and serves no public policy objective. The WMBAA believes that the Commission's regulatory interests related to SEF activities should only relate to those activities for which a SEF performs under its registration – i.e., arrangement and execution of a swap transaction. Once executed, a SEF has no ongoing obligations or interests related to a swap executed on its facility which may have a life of 30 or more years. Moreover, following execution of a swap, the SEF likely would not be made aware of its termination, which is at the discretion of the counterparties to the trade. Accordingly, it is impracticable for a SEF to definitively ascertain the period of time for which it must retain records for a particular swap that could be terminated at any time. Developing procedures to keep track of swap terminations and retain records for as long as 30 or more years after execution would result in significant and burdensome recordkeeping costs that accomplish no meaningful public policy goals. In that regard, requiring SEFs to maintain such records is not only costly and impractical, it is redundant. The SDR and the counterparties to the swap are required to retain records for the swap

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[86] J. Christopher Giancarlo, *Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank*, U.S. Commodity Futures Trading Commission (Jan. 29, 2015), at 37, https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/sefwhitepaper012915.pdf.

[87] 17 CFR 45.2(c).

until five years after its termination. Thus, the Commission can obtain necessary information related to a particular swap from the SDR or the reporting counterparty.

Accordingly, the Commission should amend its recordkeeping provisions in § 45.2(c) such that SEFs must retain records required pursuant to that section for a period of at least five years after execution of the swap rather than five years after the swap's final termination. This would provide the Commission with necessary information related to activities on the SEF to carry out its oversight responsibilities.

(3) Floor Trader Exemption

The WMBAA encourages the Commission to more accurately tailor the swap dealer registration requirement so that new liquidity providers may enter the market without the unnecessary requirement to register as a swap dealer solely based on notional value of swaps traded. The issue has arisen because the Commission stated, in adopting the swap dealer definition, that "each swap that the person enters into in its capacity as a floor trader . . . shall not be considered for purpose of determining whether the person is a swap dealer" if the swap meets a series of eight specific conditions.[88] One of those conditions is that the floor trader "[e]nters into swaps with proprietary funds for that trader's own account solely on or subject to the rules of a [DCM] or [SEF] and submits each such swap for clearing to a [DCO]."[89]

As Chairman Giancarlo, Commissioner Dan Berkovitz and others have pointed out, this provision has created ambiguity and has been the source of confusion among market participants. The existing interpretation and lack of regulatory certainty has adversely affected liquidity in swaps markets because it has discouraged potential market makers from participating in these markets. Addressing this matter through rulemaking or no-action relief would promote participation in the swaps markets as additional floor traders become eligible to rely upon the exclusion, thereby resulting in increased liquidity and more competitive prices. Accordingly, the WMBAA recommends that the Commission amend the floor trader provision, through this interpretation or other means, so that the proprietary market makers can become an alternative source of liquidity for trading on SEFs.

(4) Margin Requirements for Financial Swaps

Section 39.13(g)(2) states, in part, that a DCO shall establish initial margin requirements that are commensurate with the risks of each product and portfolio and shall use models that generate initial margin sufficient to cover its potential exposures "based on price movements in the interval between the last collection of variation margin and the time within which the derivatives organization estimates that it would be able to liquidate a defaulting clearing member's positions (liquidation time)."[90] The Commission further stipulates minimum liquidation times of one day for futures and options, including financial futures and options, and five days for all swaps that are not based on agricultural, energy, or metal commodities. Thus, the Commission's rules provide

[88] 17 CFR 1.3, Swap dealer, paragraph (6)(iv).
[89] 17 CFR 1.3, Swap dealer, paragraph (6)(iv)(B).
[90] 17 CFR 39.13(g)(2).

for a five-day margin liquidation period for financial swaps, while financial futures have a one-day margin liquidation period.

The WMBAA recommends that the Commission re-examine its margin requirements established in Part 39 for financial swaps so that they specify a realistic liquidation time period. The existing margin provisions result in a significant commercial advantage for financial futures over economically similar financial swaps. The WMBAA believes that margin requirements should be based on the economic characteristics of the products, rather than on whether a product is classified as a future or a swap. Products (like futures and swaps based on the same underlying commodity or financial instrument) have similar risk profiles and should have the same margin requirements. The Commission should recognize that swaps and futures are economically equivalent, in that a swap transaction essentially is a promise to exchange payments in the future, while a futures contract represents an obligation to make or take delivery or make a payment at a future date.

IV. CONCLUSION

The WMBAA appreciates the opportunity to comment on the Proposed Rule. We look forward to continuing to work with the Commission and its staff on all matters pertaining to SEFs, including on this and on any future CFTC rulemakings, amendments, guidance, or interpretations related to trade execution and SEFs, to ensure that the regulations are implemented in accordance with the underlying statutory intent of the Dodd-Frank Act. Please feel free to contact the undersigned with any questions you may have on our comments.

Sincerely,

Shawn Bernardo
Chairman, WMBAA