WMBA
AMERICAS
WHOLESALE MARKETS BROKERS' ASSOCIATION

March 22, 2011

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

Re: Risk Management Requirements for Derivatives Clearing Organizations
76 Fed. Reg. 3698 (January 20, 2011) – RIN 3038–AC98

Dear Mr. Stawick:

The Wholesale Market Brokers' Association, Americas ("WMBAA" or "Association")[1] is submitting this letter in response to the request for comment with respect to the rule proposal by the Commodity Futures Trading Commission (the "Commission") regarding risk management requirements for derivatives clearing organizations ("DCOs").[2] In short, and as discussed in more detail below, the Association believes that this proposal could require DCOs to violate Section 2(h)(1)(B) of the Commodity Exchange Act (the "Act") as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") by requiring them to impose higher margin requirements on swaps that are executed on swap execution facilities ("SEFs") than on identical swaps that are executed on designated contract markets ("DCMs").[3]

The WMBAA is mindful of any potential disadvantage to SEFs, such as the imposition of higher margin requirements. In a similar fashion, the WMBAA reminds the Commission that DCOs must "provide for non-discriminatory clearing of a swap . . . executed bilaterally or on or through the rules of an unaffiliated designated contract market or swap execution facility."[4] It is necessary that the rules implementing Dodd-Frank follow this clear direction and do not frustrate Congress's intent to promote competition between SEFs and DCMs with respect to the trading of swaps. An important part of the competitive landscape is that DCOs accept trades from all execution platforms and not advantage certain trading systems or platforms over others. The Commission must be sure to promulgate rules that encourage competition and are in compliance with the Act's unambiguous provision on this issue.

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

2 *See* 76 Fed. Reg. 3698 (January 20, 2011) (the "Proposing Release").

3 One of the WMBAA member firms, GFI Group Inc. ("GFI"), has previously commented on this matter in a prior letter. *See* letter from Scott Pintoff, General Counsel, GFI, to David A. Stawick, Secretary, Commission, dated February 2, 2011. This letter from the WMBAA supplements the comments made by GFI in the prior letter.

4 Act Section 2(h)(1)(B)(ii).

As noted in the Proposing Release, proposed Regulation 39.13(g)(2) (the "Proposed Rule") would require a DCO to use a five-business day liquidation horizon for cleared swaps that are not executed on a DCM, but would permit a DCO to use a one-business day liquidation horizon for all other products that it clears, including swaps that are executed on an affiliated DCM. The Proposing Release explains that, while the one-business day standard is the current standard that DCOs generally apply to futures and options on futures contracts, a minimum of five business days is appropriate for cleared swaps that are not executed on a DCM because such a time period may be necessary to close out swaps in a cost-effective manner.

The WMBAA believes that this disparity is ill-founded, given the liquidity for many of the swap products that are currently traded by wholesale brokers that are expected to register as SEFs. More fundamentally, the WMBAA believes that this disparity is inconsistent with the provisions of Section 2(h)(1)(B) of the Act. As the Commission is aware, Section 2(h)(1)(B) requires a DCO that seeks to clear swaps to adopt rules providing that all such swaps with the same "terms and conditions" are to be treated as though they are economically equivalent within the DCO. Although the phrase "terms and conditions" is not defined in the Act, the Association believes that this term clearly is intended to refer to the economic attributes of a given swap, and not to the regulatory classification of the trading facility on which a swap is executed.[5] Therefore, by mandating that DCOs treat swaps that are economically equivalent in a dissimilar manner, the WMBAA believes that the Proposed Rule could have the unintended consequence of requiring DCOs to treat economically equivalent products differently, in violation of the Act.

The WMBAA also believes that eliminating the disparity described above is consistent with the competitive landscape that Congress intended to establish for SEFs and DCMs. As the Commission has previously observed, Dodd-Frank is designed to encourage competition between SEFs and DCMs with respect to the trading of swaps, in part by rejecting the "vertical silo" model that has traditionally been employed in the futures markets.[6] The Act, as amended by Dodd-Frank, permits the same swap to be traded on a SEF or a DCM, and contemplates that multiple SEFs and DCMs may trade the same swap.[7] The Proposed Rule is, to that extent, inconsistent with Dodd-Frank because the divergent margin requirements that would result make it highly unlikely that any such competition would occur.

Accordingly, the WMBAA reiterates our request that the Commission revise the Proposed Rule to permit a DCO to determine the appropriate liquidation horizon for cleared swaps, subject to the one-day minimum standard set forth in the Proposed Rule and in accordance with its obligation under the Act to treat economically equivalent products similarly within the DCO. This approach would permit a DCO to collect margin in a prudent manner without penalizing market participants that may desire to effect swap transactions on a SEF rather than on a DCM. It would also give

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5 For example, under proposed Regulation 40.1(j), the phrase "terms and conditions" of a swap cleared by a derivatives clearing organization includes, but is not limited to, the following specifications: (i) notional values; (ii) relevant dates, tenor, and day count conventions; (iii) index; (iv) relevant prices, rates or coupons; (v) currency; (vi) stub, premium, or initial cash flow components along with subsequent life cycle events; (vii) payment and reset frequency; (viii) business calendars; (ix) accrual type; and (x) spread or points. *See* 75 Fed. Reg. 67282, 67292-93 (November 2, 2010).

6 *See* 75 FR 63732, 63745 (October 18, 2010).

7 *Id.*

effect to Congress's intent to promote competition between SEFs and DCMs with respect to the trading of swaps.

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

Sincerely,

Stephen Merkel
Chairman, WMBAA

cc: Honorable Gary Gensler
Honorable Michael Dunn
Honorable Jill E. Sommers
Honorable Bart Chilton
Honorable Scott O'Malia