MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

February 13, 2012

Via Electronic Submission: http://comments.cftc.gov

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

Re: CFTC Further Notice of Proposed Rulemaking on Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade (RIN 3038–AD18)

Dear Mr. Stawick:

Managed Funds Association ("**MFA**")[1] appreciates the opportunity to provide comments to the Commodity Futures Trading Commission (the "**Commission**") on its proposed rules related to "Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade" (the "**Proposed Rules**")[2] under Title VII[3] of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**").[4]

Executive Summary

MFA supports the Commission's establishment of a separate determination process for a designated contract market ("**DCM**") or swap execution facility ("**SEF**") to "make a swap available to trade" ("**MAT**"), as set forth in new Section 2(h)(8) of the Commodity Exchange

[1] Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and all other regions where MFA members are market participants.

[2] Further Notice of Proposed Rulemaking on "Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade", 76 Fed. Reg. 77728 (Dec. 14, 2011) (the "**Proposing Release**").

[3] Entitled "The Wall Street Transparency and Accountability Act".

[4] Pub. L. 111-203, 124 Stat. 1376 (2010).

Act ("**CEA**"), and agrees with the factors that the Commission has proposed for consideration during the determination process.[5]

MFA respectfully suggests that the Proposed Rules would be strengthened and improved by:

- **Ensuring the MAT determination is distinct and supplemental to the review of swaps for mandatory clearing**: MFA strongly agrees that the MAT determination process should be a separate process from the Commission's process for review of swaps for mandatory clearing, given the importance to the swap markets of the careful application of the MAT Criteria, which are distinct from, and in some cases, set thresholds above and beyond the five factors required under the Commission's process for review of swaps for mandatory clearing.

- **Strengthening the review process of whether or not a swap should continue to be available to trade**: MFA strongly believes that the Commission should establish and administer a clear process for determining when a swap is no longer available to trade on a DCM or SEF (referred to herein as a "**de-MAT determination**"), based on the same MAT Criteria.

- **Eliminating the provisions related to the definition of an "economically equivalent swap"**: MFA is concerned that a SEF or DCM may have economic or competitive incentives to broadly construe the meaning of an "economically equivalent swap" in a MAT determination in order to maximize the number of swaps that are made available to trade on its platform. Therefore, we recommend that the Commission eliminate the definition of an "economically equivalent swap" from the final rulemaking.

I. The MAT Determination Process Should be Separate from the Clearing Determination Process

Section 723 of the Dodd-Frank Act[6] provides that all swaps and related transactions subject to the mandatory clearing requirement and that a DCM or SEF makes "available to trade" must be traded on a DCM or SEF (the "**Mandatory Execution Requirement**"). The Commission must determine a swap's eligibility for clearing based on the application of five statutory factors, including, as one factor, the existence of significant outstanding notional

[5] To make a MAT determination for a swap for purposes of Section 2(h)(8) of the CEA, the Proposed Rules would require a DCM or SEF to consider any one or more of the following liquidity-related factors: (1) whether there are ready and willing buyers and sellers; (2) the frequency or size of transactions on DCMs, SEFs, or of bilateral transactions; (3) the trading volume on DCMs, SEFs, or of bilateral transactions; (4) the number and type of market participants; (5) the bid/ask spread; (6) the usual number of resting firm or indicative bids and offers; (7) whether a DCM's trading facility or a SEF's trading system or platform will support trading in the swap; or (8) any other factor that the DCM or SEF may consider relevant. Proposing Release at 77732. In this letter, we collectively refer to these eight factors as the "**MAT Criteria**".

[6] Section 723(a)(3) of the Dodd-Frank Act amends the CEA to add Section 2(h)(8)(B) of the CEA.

exposures, trading liquidity and adequate pricing data.[7] MFA strongly believes that the determination of whether a clearing-eligible swap is suitable for the Mandatory Execution Requirement requires a separate process to enable a more granular application and assessment of the Commission's proposed MAT Criteria related to that swap. MFA strongly believes that a clearing-eligible swap does not necessarily equate to its suitability for mandatory trading on SEFs and DCMs, particularly due to the sporadic or discontinuous liquidity in some swap markets.[8] We urge the Commission to retain its proposed separate process for a MAT determination and objectively inform that process by reviewing a swap's trading data reported to swap data repositories for trades effected both on and off a SEF or DCM.[9]

MFA is concerned that a simultaneous process for mandatory clearing determinations and MAT determinations would unnecessarily complicate or delay the review of swaps for mandatory clearing. The implementation of central clearing and the delivery of its systemic risk reducing benefits need not be complicated and delayed by trade execution issues concerning the appropriate scope, modes, or venues of execution requirements. MFA is very concerned that linking the processes for clearing determinations and MAT determinations will complicate and delay the transition to central clearing.[10]

We are also concerned that a simultaneous process would result in inadequate assessments of the MAT Criteria, and would rush MAT determinations, with significant adverse effects on market participants. Wrapping the MAT determination process into the clearing determination process would lead to premature MAT determinations without adequate time for Commission review and public comment to ensure that a swap has sufficient liquidity and is thus suitable for the Mandatory Execution Requirement. MFA believes that a separate process with adequate Commission oversight in reviewing MAT determination submissions by DCMs and SEFs will mitigate the adverse market effects of a first-mover advantage in which a single SEF or DCM could disproportionately and anti-competitively benefit from being the first mandatory trading venue for a particular swap.[11] Moreover, because the MAT determination could remove

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7 "Process for Review of Swaps for Mandatory Clearing", 76 Fed. Reg. 44464 (July 26, 2011). The five factors are set forth on p. 44473.

8 We are specifically referring to the fact that swap markets feature a broad offering of less-standardized products as well as larger-sized orders that are traded by fewer counterparties.

9 *See supra*, note 5.

10 *See also* MFA's comments on the Commission's Notice of Proposed Rulemaking on "Swap Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA", 76 Fed. Reg. 58186 (Sept. 20, 2011) filed with the Commission on November 4, 2011, available at: http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=49947 (advocating for the transition to clearing to proceed before the separate transition to SEF/DCM execution to avoid further delay in implementing central clearing).

11 *See also* MFA's comments on the Commission's Notice of Proposed Rulemaking on "Core Principles and Other Requirements for Swap Execution Facilities", 76 Fed. Reg. 1214 (Jan. 7, 2011) filed with the Commission on March 8, 2011, available at: http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=31242 (expressing

a swap from the over-the-counter ("**OTC**") market, it could effectively preclude a significant segment of customers, including many MFA fund members, and market makers without connectivity to the relevant SEF platform from entering the market in that swap. Therefore, market participants would have to seek connectivity with that SEF platform in order to trade the swap, which would give an advantage to market participants with greater resources to devote to information technology connectivity, operations and document negotiation. The exclusion from trading of market participants that do not have such resources would be contrary to the equal access considerations of the Dodd-Frank Act.[12] To minimize this exclusionary effect, we believe that all market participants should have a 90-day implementation period before a final MAT determination becomes effective.

II. The Commission Should Establish a Process for de-MAT Determinations

We appreciate that the Commission has recognized that a swap's MAT determination is a fluid determination which requires regular reassessments by SEFs and DCMs to determine whether a SEF or DCM should continue to make that swap available for trading.[13] To reinforce that recognition, MFA recommends that the Commission should establish and administer a clear process for de-MAT determinations. We strongly believe that the economic incentives faced by DCMs and SEFs to continue to make a swap available to trade may not lend the requisite objectivity to the annual reviews and assessments submitted by DCMs and SEFs to the Commission. Regardless of a DCM's or SEF's incentives, the Commission will have a broader view of the market liquidity of a swap than an individual DCM or SEF will have by virtue of the trading data submitted to the Commission pursuant to the final transaction reporting and swap data repository rules. Thus, we believe the Commission should review those data and not rely exclusively on an individual DCM's or SEF's annual self-assessment or self-certification that a swap continues to trade effectively on its own platform.

Accordingly, we urge the Commission to specify a periodic process to revisit the trading characteristics of a given swap product based on the Commission's consideration of the same MAT Criteria as are required for its consideration of a MAT determination submission. If that product is no longer trading effectively in a DCM or SEF environment, as confirmed objectively by the Commission's broader view of market trading data for the product in question, the Commission should suspend the Mandatory Execution Requirement for that product, with

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concern with the potential first-mover monopoly risk posed by an individual SEF's discretionary MAT determination).

[12] *See* Section 733 of the Dodd-Frank Act, amending the CEA to introduce Section 5h(f)(2)(B)(i), requiring SEFs to establish rules that "provide market participants with impartial access to the market".

[13] Proposing Release at 77732 ("Regular reviews help ensure that DCMs and SEFs routinely evaluate whether swaps previously determined to be available to trade should continue to be treated in that manner.").

universal application of the suspension to all DCMs and SEFs and public notification to provide market certainty.[14]

III. The Definition of "Economically Equivalent Swap" Should be Eliminated from Both Processes

MFA believes that the proposed definition of the term "economically equivalent swap" [15] should be eliminated from the final rules for purposes of both MAT determinations and de-MAT determinations. We believe the definition would lend too much subjectivity to both processes, and create market uncertainty as to the universe of swaps that is subject to the Mandatory Execution Requirement at any given point in time. MFA is concerned with the economic and competitive incentives of a SEF or DCM to broadly construe the meaning of an "economically equivalent swap" in a MAT determination for a particular swap product, particularly given their incentives to maximize the number and types of MAT-eligible swaps on their platforms. We believe the proposed definition would inappropriately expand the universe of swaps that are subject to the Mandatory Execution Requirement, without any opportunity for formal Commission review or public comment to ensure that economically equivalent swaps, as determined by DCMs or SEFs, actually meet the MAT Criteria and can trade effectively in a DCM or SEF environment. If a particular swap product has similar or equivalent economic terms to a MAT-eligible swap, that swap should undergo the same MAT determination process. Moreover, we believe the inclusion of the "economically equivalent swap" construct in the final rulemaking would add unnecessary regulatory complexity and administrative burdens for Commission staff. Accordingly, MFA recommends that the Commission eliminate the provisions related to the definition of an "economically equivalent swap" from the final rulemaking.

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[14] Given that the de-Mat determination process should not affect a swap's clearing eligibility, MFA believes that the need for a separate process for determining a swap's MAT eligibility is further underscored.

[15] The Proposed Rules define an "economically equivalent swap" as a swap that the SEF or DCM "determines to be economically equivalent with another swap after consideration of each swap's material pricing terms". Proposing Release at 77737.

MFA thanks the Commission for the opportunity to provide comments regarding the Proposed Rules. Please do not hesitate to contact Laura Harper or the undersigned at (202) 730-2600 with any questions the Commission or its staff might have regarding this letter.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director, General Counsel

cc: The Hon. Gary Gensler, Chairman
The Hon. Jill E. Sommers, Commissioner
The Hon. Bart Chilton, Commissioner
The Hon. Scott D. O'Malia, Commissioner
The Hon. Mark P. Wetjen, Commissioner