

August 1, 2012

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

Re: Proposed Rules Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades (RIN 3038-AD84)

Dear Mr. Stawick:

The Wholesale Market Brokers' Association, Americas ("WMBAA" or "Association")¹ appreciates the opportunity to provide specific comments to the Commodity Futures Trading Commission ("CFTC" or "Commission") related to the proposed rules prohibiting the aggregation of orders to satisfy minimum block sizes or cap size requirements, and establishing eligibility requirements for parties to block trades ("Proposed Rules")² under the Commodities Exchange Act ("CEA"), as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").

This letter supplements prior comments provided by the WMBAA to the Commission in response to its Proposed Rules.³ As previously indicated, the WMBAA is supportive of a regulatory regime for over-the-counter ("OTC") swaps markets that improves regulatory transparency, promotes competition, and fosters market participant access to a vibrant, affordable source of liquidity. The WMBAA supports transparency in OTC swaps markets for all market participants. WMBAA members' trade execution platforms provide their participants with the most current market information for the express purpose of price discovery and the matching of buyers and sellers, using knowledgeable brokers and sophisticated electronic trading and matching systems to create greater trading liquidity.

¹ The WMBAA is an independent industry body representing the largest inter-dealer brokers operating in the North American wholesale markets across a broad range of financial products. The five founding members of the group are: BGC Partners; GFI Group; ICAP; Tradition; and Tullett Prebon. 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. For more information, please see <http://www.wmbaa.org>.

² See Rules Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades, 77 Fed. Reg. 38229 (June 27, 2012).

³ See, e.g., letter from J. Christopher Giancarlo, Chairman, WMBAA, to Commission and CFTC, dated July 29, 2010; see also letter from Julian Harding, Chairman, WMBAA, to Commission and CFTC, dated Nov. 19, 2010; letter from Julian Harding, Chairman, WMBAA, to Commission and CFTC, dated Nov. 30, 2010; letter from Julian Harding, Chairman, WMBAA, to Commission, dated Jan. 18, 2011; letter from Christopher Ferreri, Chairman, WMBAA, to Commission, dated May 8, 2012; letter from Christopher Ferreri, Chairman, WMBAA, to Commission, dated May 14, 2012.

Overview

This letter provides additional information on the concept of “work-up” and explains its vital role in liquidity formation in OTC swaps markets.

Additionally, as a general principle, the WMBAA urges the Commission to recognize the significant differences between futures markets and OTC swaps markets, including the number of products traded, the average daily trading volume, and, importantly, the distinct statutory regimes.

The Commission’s implementing rules for the swaps market must take into consideration the significant differences between the trading of futures on an existing futures exchange and the trading of swaps on SEF platforms. While it may be appropriate to look to the futures model as instructive in certain instances, overreliance on that model will not achieve Congress’ goal. Congress explicitly incorporated a SEF alternative to the exchange-trading model, understanding that competitive execution platforms provide a valuable market function. Rules governing SEFs and SEF trading should reflect Congressional intent and promote the growth of existing competitive, vibrant markets without impeding liquidity formation.

For these reasons, the WMBAA encourages the CFTC to clarify in the Proposed Rules its intent, as further discussed below, to prohibit the aggregation of orders for specific trading accounts and not to impede liquidity formation by preventing the use of “work up” in OTC swaps activity.

Work-up Is a Valuable Component of Liquidity Creation

WMBAA member firms have witnessed an evolution in interdealer markets with the development of a process referred to as “work-up.” In this model, once a price is agreed upon for trading, the resultant trade is reported to market participants and they are offered the opportunity for a brief period of time to “join the trade” by placing a firm bid or offer that is characterized by only two variables (the quantity and whether the order is a “buy” or “sell” order). This results in an increase in liquidity at the most recently established market price.

It is vital that any block trade calculation recognize the role that work-up plays in forming liquidity. Work-up enables market participants to assess the markets in real-time and make real-time decisions on trading activity without the fear of moving the market one way or another. This is done to allow the market to find the appropriate pricing levels to optimally complete the transaction without prematurely causing the market impact of a large block trade.⁴

During the “work-up” or “join the trade” period, all market participants have knowledge that a trade is taking place and are welcome to participate in this transparent process. However, as the initiating trade and other trades that take place are not fully complete until the end of the work-up period, and

⁴ 156 Cong. Rec. S5921 (daily ed. July 15, 2010) (Statement of Sen. Blanche Lincoln) (“Block trades, which are transactions involving a very large number of shares or dollar amount of a particular security or commodity and which transactions could move the market price for the security or contract, are very common in the securities and futures markets. Block trades, which are normally arranged privately, off exchange, are subject to certain minimum size requirements and time delayed reporting.”).

may result in both block and non-block trades, the block trade calculations should not be done until the brief work-up period expires.

Aggregation of Orders for Different Accounts Distinct from Work-up

The WMBAA believes that the Commission's intent to prohibit the "aggregation of orders for different accounts in order to satisfy the minimum block trade size or the cap size requirement" specified in proposed section 43.6(h)(6) does not relate to the concept of "work-up" as described above. Rather, the Commission seems focused on specific trading accounts maintained, for example, by a buy-side firm for its customers. As commenters have indicated, "[a]sset managers invest money for clients, typically in funds or separate accounts."⁵ This concept also extends to investment advisers who manage trading accounts for separate customers.⁶

The WMBAA respectfully requests that the Commission clarify that it does not intend to extend the reach of the Proposed Rules to trades resulting from being "worked-up" through a conventional market mechanism. The prohibition on aggregation of orders for different accounts can be implemented without a prohibition on aggregating resulting swaps that are produced by market participants joining a trade and executing at the price established at that time.

Practical Implications of Prohibiting Work-up

The WMBAA believes that prohibiting "work-up" will have significantly harmful implications for OTC swaps markets, to the detriment of market participants in the form of wider bid-ask spreads, less trading volume, and less transparent price discovery.

Similarly, the WMBAA believes there are several real-world situations not addressed by the Proposed Rules' application, as the following examples illustrate. The WMBAA asks that the Commission, through discussion in the preamble to the Proposed Rules, interpretive guidance, or otherwise, provide guidance for compliance with Part 43 rules for certain fact-specific instances such as the following.

To demonstrate these situations, assume for these purposes that there is a block trade threshold of 100 for a certain swap.

Example 1

- Party A submits an order to a voice broker SEF to buy a swap at a certain price, size of 100. Party B communicates to the voice broker that he will sell the swap at the price in a size of 100. This appears to consummate a block trade.

⁵ See letter from Joanne Medero and Richard Prager, Blackrock, June 3.
<http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=44664&SearchText=institutional%20investor>.

⁶ See letter from American Benefits Council and the Committee on the Investment of Employee Benefit Assets, Feb. 7, 2011 ("Qualified investment advisers who are not commodity trading advisers should be able to aggregate block trade orders for different trading accounts.")

- Party B instantly bids another 50 of the same swap at the same price. If Party A accepts the bid and buys an additional 50, the resulting trade could be considered one block trade of 150. In the alternative, two transactions might be recognized – one a block trade, and the other not a block trade. The Commission’s treatment of this example will have significant impact on liquidity formation. The WMBAA believes, and requests that the Commission clarify, that the Proposed Rules would not impact “work-up” and the activity above would result in one reported block trade (on a delayed basis) of a size of 150.

Example 2

- Party A submits an order to a voice broker SEF to buy a swap at a certain price, size of 100. Party B communicates to the voice broker that he will sell the swap at the price in a size of 75. The transaction is consummated at 75. The initial price-forming bid would qualify for a block trade. It remains unclear whether the initial bid above the block trade threshold would permit the executed swap (below the block trade threshold) to receive block trade treatment.

Example 3

- Party A submits an order to a voice broker SEF to buy a swap at a certain price, size of 100. Party B communicates to the voice broker that he will sell the swap at the price in a size of 75. Party C communicates to the voice broker that he will sell the swap at the price in a size of 75 as well. Party A agrees to buy the swap at the price in a size of 75 from both Party B and Party C. From the perspective of Party A, it has bought 150. The WMBAA believes, and requests that the Commission clarify, that the Proposed Rules would not impact “work-up” and the activity above would result in one reported block trade (on a delayed basis) of a size of 150.

Conclusion

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

Sincerely,



Christopher Giancarlo
Chairman, WMBAA
Executive Vice President, GFI Group Inc.