



| asset management group

December 2, 2013

Ms. Melissa Jurgens  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street NW  
Washington, DC 20581

**Re: Javelin SEF, LLC Made Available to Trade Determination (Industry Filing 13-06)**

Dear Ms. Jurgens:

The Asset Management Group<sup>1</sup> (“AMG”) of the Securities Industry and Financial Markets Association (“SIFMA”) appreciates the opportunity to provide the Commodity Futures Trading Commission (the “Commission”) with comments regarding the Javelin SEF, LLC’s (“Javelin”) “determination” that certain interest rate swaps are “made available to trade” (“MAT”) and should therefore become subject to the trade execution requirement of the Dodd–Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”). On November 29, 2013, AMG received notification from Javelin that it had amended their October 12, 2013 “determination”<sup>2</sup> (“October MAT Determination”) by radically narrowing the scope of contracts intended to be MAT.<sup>3</sup> The comment period for the October MAT Determination was scheduled to close on December 2, 2013 and we were prepared to submit a comment letter raising serious concerns with the October MAT Determination on that date. We expect that the Commission

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<sup>1</sup> The AMG’s members represent U.S. asset management firms whose combined assets under management exceed \$20 trillion. The clients of AMG member firms include, among others, registered investment companies, ERISA plans, and state and local government pension funds, many of whom invest in commodity futures, options, and swaps as part of their respective investment strategies.

<sup>2</sup> Javelin Determination of Made Available to Trade of Certain Interest Rate Swaps Made Available to Trade Pursuant to Parts 37 of the Rules of the Commodity Futures Trading Commission (Submission No. 13-06R) (Oct. 18, 2013, revised Oct. 31, 2013).

<sup>3</sup> See Javelin SEF Streamlines its Interest Rate Swap MAT Submission Citing Operational Readiness Concerns, <http://www.thejavelin.com/press-releases/Javelin+SEF+Streamlines+its+Interest+Rate+Swap+MAT+Submission> (Nov. 29). For example, the interest rate swap tenors covered by the November submission represents less than 0.08% of the tenors covered by the October MAT Determination. More explicitly, the October MAT determination covered over 11,315 interest rate swap tenors in three currencies (U.S. dollar, Euro, and British pound) while Javelin’s November 29 revised determination covers eight specific “benchmark tenors,” (two, three, five, seven, ten, 15, 20, and 30 year tenors) in two currencies (U.S. dollar and Euros). Compare October MAT Determination, at 7 with Javelin Determination of Made Available to Trade of Certain Interest Rate Swaps Made Available to Trade Pursuant to Parts 37 of the Rules of the Commodity Futures Trading Commission (Submission No. 13-06R(2)) (Oct. 18, 2013, revised Oct. 31, 2013 further revised Nov. 29, 2013) (“November MAT Determination”), at 7.

will now open a 30-day comment period for this new submission and restart the 90-day review period under Commission regulation 40.6(c) for this latest submission because the revisions that Javelin has made essentially amount to an entirely different rule that Javelin is certifying.

The AMG supports an orderly transition to the Commission's new trade execution requirement paradigm. However, market participants, including AMG's members, will be at significant risk of harm if that transition is not managed properly. As we will detail in a separate letter to the Commission, we urge the Commission to undertake a carefully phased implementation.

We are pleased that Javelin has acknowledged the concerns that we and other participants had with its overbroad October MAT Determination by narrowing its scope significantly, and we commend Javelin for amending the October MAT Determination. We were of the opinion that the October MAT Determination should have been rejected by the Commission for failing to make a sufficient showing for the swaps covered thereunder. As our comments on the October MAT Determination address important issues that may be repeated by overly ambitious swap execution facilities ("SEFs") in the future and as the November MAT Determination has retained much of the analysis used by Javelin in the October MAT Determination,<sup>4</sup> we believe that our comments on Javelin's October MAT Determination will still be helpful to the Commission as it reviews current and future MAT determinations. We are therefore providing comments on Javelin's October MAT Determination below.<sup>5</sup>

#### **AMG Comments on October MAT Determination:**

The AMG agrees with the Commission that Javelin's October MAT Determination presents novel or complex issues and therefore warrants opportunity for public comment and careful Commission review.<sup>6</sup> There is a misconception held by some that a MAT determination is a virtual *fait accompli* upon submission. As described in further detail below, we believe this view is contrary to the Commission's rules, the Commodity Exchange Act ("CEA" or "Act"), and the policy guiding the Commission's rules. The Commission has stated that the MAT determination process, including Commission review of MAT determinations, would serve as a "backstop" against the significant costs borne by the public if illiquid swaps are "made available to trade." We believe Javelin's October MAT Determination fails to meet the listing requirement of Commission regulation 37.10(a)(2)(ii) by not demonstrating that it can "support trading" in all of the swaps covered therein. The October MAT Determination also fails to properly "consider" the factors required for a MAT determination as required under the "factors to consider" requirement of Commission regulation 37.10(b) with respect to *all* the swaps within

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<sup>4</sup> Compare e.g., October MAT Determination, at 13-14 discussed in *infra* section III(b) below with November MAT Determination, at 13-15.

<sup>5</sup> AMG reserves the right to submit further comment on Javelin's November 29 submission in any new comment period provided by the Commission.

<sup>6</sup> Cf. 17 CFR 40.6(c) and CFTC PR 6742-13 (Oct. 18, 2013), available at <http://www.cftc.gov/PressRoom/PressReleases/pr6742-13>.

its expansive scope. In addition, the Commission must assure that MAT determinations demonstrate sufficient trading liquidity to support the requested expansion of the trade execution requirement.

### **I. Need for sufficient trading liquidity**

The Dodd-Frank Act provides that once a swap subject to the Commission's clearing requirement is "made available to trade" by a SEF or designated contract market ("DCM"), it becomes subject to the Commission's trade execution requirement.<sup>7</sup> In the final rulemaking promulgating standards governing MAT determinations (the "MAT Rulemaking"),<sup>8</sup> the Commission interpreted this statutory language to support "an available-to-trade determination that is separate from a mandatory clearing determination."<sup>9</sup> Though the factors to be considered may sometimes be similar, the fact that a swap is determined to be subject to the clearing requirements does not mean that it has been determined to be subject to the trade execution mandate. Rather, a different analysis is to be undertaken.

Consistent with this statutory interpretation, the Commission has set forth separate and distinct liquidity-related criteria for the clearing and trade execution requirements. The Commission explained that while the "focus" of a MAT determination may be on "whether a swap has sufficient trading liquidity to be subject to mandatory trade execution,"<sup>10</sup> clearing requirement determinations are not focused on "the liquidity of specific individual swaps."<sup>11</sup> Liquidity in the clearing requirement context focuses on risk management and "whether a portfolio of swaps has common specifications that are determinative of their economic characteristics, such that a [derivatives clearing organization] can price and risk manage the portfolio in a default situation."<sup>12</sup> In contrast, Commission regulation 37.10(b) sets forth factors to be considered in making a MAT determination, "each of [which] is an indicator of *trading activity*" in a swap.<sup>13</sup> The Commission, therefore, has interpreted the CEA to apply the trade execution requirement to a subset of the swaps that are subject to the clearing requirement that have trading activity that would be supported in a "centralized trading environment."<sup>14</sup>

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<sup>7</sup> Section 723(a)(3) of the Dodd-Frank Act added section 2(h)(8) of the CEA to require that swap transactions subject to the clearing requirement must be traded on either a DCM or SEF, unless no DCM or SEF "makes the swap available to trade" or the transaction is not subject to the clearing requirement under section 2(h)(7).

<sup>8</sup> Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act, 78 Fed. Reg. 33,606.

<sup>9</sup> 78 Fed. Reg. at 33,609.

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 33,613 (emphasis added).

<sup>14</sup> *Id.*

The distinction between liquidity sufficient to support a clearing requirement determination versus liquidity sufficient to support a MAT determination is at the heart of the MAT Rulemaking. In the MAT Rulemaking, the Commission acknowledged concerns about the “costs imposed upon market participants if *illiquid* swaps [subject to the clearing requirement] are made available to trade and become subject to the trade execution requirement.”<sup>15</sup> These costs to the public, including AMG members, consist of increased transaction costs and diminished liquidity that would follow from an overly broad MAT determination.<sup>16</sup> The Commission assured commenters to its proposed rulemaking, however, that the transparency of the MAT determination process “coupled with *Commission review* and potential for public comment, provides an important *backstop* to protect the integrity of the determinations that are submitted.”<sup>17</sup>

We believe the Commission should apply the MAT backstop it promised the public by rejecting MAT determinations that are not procedurally and substantively warranted. If the Commission reviews a MAT Determination under a standard that amounts to a “check the box” review merely for apparent completeness, then it would effectively nullify the statutory “make[] the swap available to trade” requirement. We do not believe this is consistent with the standards the Commission has set forth for MAT determinations, as discussed further below.

## **II. A MAT determination must meet the listing requirement by demonstrating that the submitting SEF can support trading in swaps it intends to make “available to trade”**

The Commission may deny a MAT determination if it violates the CEA or Commission regulations.<sup>18</sup> Commission regulation 37.10(a)(2) sets forth a listing requirement for swaps that a SEF makes “available to trade.”<sup>19</sup> In order for a SEF to comply with the listing requirement, its MAT determination “must demonstrate that it lists or offers that swap for trading on its trading system or platform.”<sup>20</sup> This must include whether the SEF “supports trading” in such a swap.<sup>21</sup>

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<sup>15</sup> *Id.* at 33,622 (emphasis added).

<sup>16</sup> AMG members would pay more to transact an illiquid swap subject to a trade execution requirement because their counterparty would charge them for the counterparty’s increased costs to offset the risk of the swap (*i.e.*, an “illiquidity premium”). Illiquidity premiums increase as a function of the illiquidity in the swap (how many willing counterparties there are, how often they transact, etc.) and the extent that the demand for liquidity is known in the market. The requirement to trade on a central limit order book or through an request for quote (“RFQ”) system would put at least two (or three) market participants on notice of a party’s demand for liquidity. In many illiquid interest rate swaps, there may not be much depth and may be only one or two willing dealer counterparties, and in those markets, AMG members would have to pay a significant illiquidity premium if the trade execution requirement is overbroad.

<sup>17</sup> 78 Fed. Reg. at 33,622 (emphasis added).

<sup>18</sup> 17 CFR 40.6(c)(3).

<sup>19</sup> 17 CFR 37.10(a)(2).

<sup>20</sup> *Id.*

In order to properly support trading in the swap, the SEF, at a minimum, must be able to support “Order Book”<sup>22</sup> trade execution.

Javelin’s October MAT Determination does not demonstrate that it supports “Order Book” trading in all the swaps within its broad expanse. Rather, the Javelin October MAT Determination merely “certifies that all Submission Swaps. . . are currently listed by Javelin” and links to a page on its website.<sup>23</sup> Yet, the webpage Javelin offers<sup>24</sup> as evidence it has “listed” the swaps in its MAT determination is not functional.

Beyond this, Javelin does not demonstrate whether it has the technological and operational capabilities to support “Order Book” trading for all of the swaps in the October MAT Determination. The October MAT Determination covers over 11,315 interest rate swap tenors.<sup>25</sup> The Commission’s MAT review backstop requires a submitting SEF to demonstrate its ability to support trading in all of the swaps contained in its MAT determination.<sup>26</sup> Further, according to data compiled by the AMG for roughly seven weeks (October 2 through November 15), Javelin accounted for less than 0.09% of swap notional amounts traded on SEFs.<sup>27</sup> To date, no other SEF has claimed an ability to support “Order Book” trading in anything more than a handful of standard tenor interest rate swaps.

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<sup>21</sup> In the MAT Rulemaking, the Commission explained that it had proposed requiring SEFs and DCMs in their MAT determinations to consider “whether a SEF’s or DCM’s trading facility or platform will support trading in the swap.” 78 Fed. Reg. at 33,613. The Commission, however, concluded that this requirement was “redundant” with the listing requirement because “[t]his factor contemplated, among other things, whether the SEF or DCM lists the swap for trading on its trading facility or platform.” *Id.* The import of this discussion is that in order to comply with the listing requirement in Commission regulation 37.10(a)(2), a SEF or DCM must consider whether it “supports trading” in the swap. Otherwise, if the requirement that a SEF or DCM supports trading in the swap is not embedded within the listing requirement and the MAT determination, then there was no redundancy and no basis for the Commission’s deletion of the proposed “supports trading” factor.

<sup>22</sup> “Order Book” is defined as “(i) An electronic trading facility, as that term is defined in section 1a(16) of the Act; (ii) A trading facility, as that term is defined in section 1a(51) of the Act; 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.” 17 CFR 37.3(a)(3).

<sup>23</sup> October MAT Determination, at 5.

<sup>24</sup> *Id.* at footnote 9 (“See website: [www.thejavelin.com/products](http://www.thejavelin.com/products).”).

<sup>25</sup> 11,315 = 365 days times 31 years. Note that there are many orders of magnitude of additional permutations of swaps covered by the October MAT Determination that are not discussed here. Interest rate swaps can have different trade dates, maturities, currencies, reference indices, payment and reset dates, etc.

<sup>26</sup> Javelin, like other SEFs, is currently only temporarily registered. Temporary registration means that the Commission has not thoroughly reviewed Javelin’s compliance with all applicable statutory and regulatory requirements, making it all the more imperative that the Commission enforce the backstop of its “made available to trade” review to assure that a temporarily-registered SEF has the capability to support trading in all swaps it claims to make available to trade. 17 CFR 37.3(c).

<sup>27</sup> Javelin accounted for \$4.35 billion notional amount while a total of \$5.07 trillion (Source: ICAP, Bloomberg, Tradeweb and Javelin) was transacted across those four SEFs.

Extending the trade execution requirement to thousands of interest rate swap tenors without a demonstration that the requesting SEF can support a functioning “Order Book” for trading them would invite a market disruption. If all of these swap tenors are made “available to trade” without requiring a demonstration that the requesting SEF has the technological and operational capacity to support “Order Book” trading in them, then market participants, including AMG members, bear the risk that they will not be able to comply with the trade execution requirement if it turns out that the requesting SEF is unable to do so.<sup>28</sup> This result would place transactions to hedge potentially trillions of dollars of interest rate risk – *i.e.* transactions by market participants the trade execution requirement was intended to benefit – in regulatory limbo. Under such circumstances, the Commission should deliver on its commitment to provide a backstop in the MAT determination process and enforce compliance with the listing requirement of Commission regulation 37.10(a)(2).

### **III. The Commission should deny a MAT determination if it fails to address relevant MAT factors for all of the swaps it contains**

In Commission regulation 37.10(b), the Commission set forth six factors (“MAT Factors”) that indicate when a swap is “available to trade.”<sup>29</sup> The MAT Rulemaking stated that it is not “necessary for a SEF or DCM to analyze and demonstrate compliance with every factor in a submission” and that, under certain circumstances, the demonstration of trading liquidity could be made through an analysis of a single factor.<sup>30</sup>

The Commission allows MAT determinations to cover groups or categories of swaps under certain specific circumstances.<sup>31</sup> In doing so, the Commission was careful to guard against an overly aggressive grouping of swaps into a single MAT determination. The Commission explicitly states that a SEF or DCM making a determination that a group or category of swaps is “available to trade” under the “factors to consider” requirement of Commission regulation 37.10(b)<sup>32</sup> “*must address*, in its submission, the applicable determination factor or factors apply to *all* of the swaps within that group [or] category . . .”<sup>33</sup> The Commission’s use of the terms “must” and “all” means that if a SEF or DCM fails to address an applicable MAT factor or factors with respect to all of the swaps in a group or category, then the SEF or DCM may not

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<sup>28</sup> Once a swap is made “available to trade” pursuant to Commission regulation 37.9, then it becomes a “Required Transaction” and market participants must execute such swaps on a SEF or DCM (unless the swap qualifies as a “block” trade pursuant to SEF or DCM rules and 17 CFR 43.6). CEA section 2(h)(8), 7 USC 2(h)(8), and 17 CFR 37.9.

<sup>29</sup> 78 Fed. Reg. at 33,613. The six MAT Factors are: (1) whether there are ready and willing buyers and sellers; (2) frequency or size of transactions; (3) trading volume; (4) number and types of market participants; (5) bid/ask spread; or (6) usual number of resting firm or indicative bids and offers. 17 CFR 37.10(b) and 17 CFR 38.12(b).

<sup>30</sup> 78 Fed. Reg. at 33,613.

<sup>31</sup> It also permits MAT determinations to cover “types” and “classes” of swaps under the same circumstances. *Id.*

<sup>32</sup> 17 CFR 37.10(b).

<sup>33</sup> 78 Fed. Reg. at 33,611 (emphasis added).



make that group or category of swaps “available to trade” under Commission regulation 37.10(b).

(a) The Commission should deny a MAT determination if it does not properly consider one or more of the MAT Factors

A SEF or DCM’s MAT determination may be denied for failure to demonstrate a swap is “available to trade” under the “factors to consider” requirement of Commission regulation 37.10 if the SEF or DCM “does not consider one or more of the required factors.”<sup>34</sup> The Commission has provided some relevant guidance as to when a SEF or DCM has properly considered relevant MAT Factors. Three points the Commission makes in the MAT Rulemaking are particularly relevant here. First, as mentioned above, the MAT Factors are intended to be “indicator[s] of *trading activity*” that may be relevant in a MAT determination.<sup>35</sup> Second, the Commission suggested its approach to MAT determinations is to allow SEFs or DCMs to “accommodate swaps with different trading characteristics that can be supported in a *centralized trading environment*.”<sup>36</sup> Finally, in its consideration of a MAT Factor, the SEF or DCM must provide “analysis and an application of the MAT Factors sufficient to demonstrate sufficient trading activity or other information that demonstrates that prospective MAT swaps can be supported in a centralized trading environment.”<sup>37</sup> An inadequate “analysis and application” of relevant MAT Factors is therefore grounds for the Commission to deny a MAT determination under the “factors to consider” requirement of Commission regulation 37.10(b).<sup>38</sup>

The MAT Rulemaking requires that the Commission effectuate the MAT review backstop by undertaking a substantive review of a SEF or DCM’s “analysis and application” of the MAT Factors. Moreover, the Commission has encouraged the use of as much information about the swaps marketplace as possible, including “[i]nformation about trading activity in the entire swaps marketplace [that] would better inform market participants about how the swap [covered by a MAT determination] trades in the overall market,” in the consideration of MAT Factors.<sup>39</sup> More comprehensive information would “provide interested parties with additional information and analysis to comment upon” and “better inform the Commission in its evaluation of the available-to-trade submission.”<sup>40</sup>

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<sup>34</sup> *Id.* at 33,610.

<sup>35</sup> *Id.* at 33,613.

<sup>36</sup> *Id.* (emphasis added)

<sup>37</sup> The Commission noted that it may find a MAT determination as contrary to the CEA and Commission regulations depending upon “the SEF’s or DCM’s analysis and application of the determination factors to the swap submitted as available to trade.” *Id.* at 33,610.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 33,612.

<sup>40</sup> *Id.*

- (b) Javelin's October MAT Determination fails to address the relevant factors for "all" of the swaps in the MAT determination as required under the "factors to consider" requirement of Commission regulation 37.10(b)

The approach taken in the October MAT Determination combining swaps into interest rate swap categories lacks the level of granularity necessary to address each MAT Factor for all swaps in its MAT determination.<sup>41</sup> Javelin's October MAT Determination combines interest rate swaps that lack trading liquidity together with some liquid swaps. It establishes three broad currency-based categories, one category for all U.S. dollar Libor interest rates with tenors of 0 to 31 years, another for British pound Libor interest rates, and another for Euro Euribor interest rates (the "Three Categories").<sup>42</sup> The October MAT Determination either applies the MAT Factors to the Three Categories either (i) in their totality and attributed liquidity traits to all swaps in each, or (ii) only applied the MAT Factors to the most liquid, standard tenor interest rate swaps in the Three Categories. In either case, Javelin does not distinguish between liquid and illiquid swaps within each category and therefore failed to address a single MAT Factor to a degree sufficient to support a MAT determination. Indeed, Javelin only specifically mentions information relating to 13 different tenors in its discussion of the MAT Factors in the October MAT Determination out of over 11,315 U.S. dollar interest rate swap tenors covered therein, *i.e.* less than 0.12% of the tenors covered in the October MAT Determination.

Javelin defends this "portfolio approach" to its Three Categories in the October MAT Determination by arguing that it "is consistent with other market practitioners such as [derivatives clearing organizations or "DCOs"] with regard to liquidity considerations and [interest rate] swaps classification."<sup>43</sup> The Commission, however, distinguished the portfolio approach to gauging liquidity that is used by DCOs from the approach to gauging liquidity for the purpose of a MAT determination.<sup>44</sup> In the MAT Rulemaking, the Commission contrasted a MAT determination's "focus" on "whether a swap has sufficient trading liquidity to be subject to mandatory trade execution" with the clearing requirement's focus on liquidity "as a function of whether a portfolio of swaps has common specifications that are determinative of their economic characteristics, such that a DCO can price and risk manage the portfolio in a default situation."<sup>45</sup> The Commission intended that the approach to gauging liquidity for the purpose of the clearing requirement would be less restrictive than the approach taken for MAT determinations.

We believe that in order for swaps to be considered together in groups for the purpose of a MAT Factor analysis, they should have in common liquidity or trading activity characteristics that would make the analysis for the group relevant to *all* of the swaps contained in the group. The swaps in each of the Three Categories in the October MAT Determination do not share

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<sup>41</sup> *Id.* at 33,613.

<sup>42</sup> October MAT Determination, at 6.

<sup>43</sup> *Id.* at 13.

<sup>44</sup> *See* 78 Fed. Reg. at 33,609.

<sup>45</sup> *Id.* at n. 56.



common liquidity or trading activity characteristics that would allow them to be able to be appropriately analyzed together under the MAT Factors. Liquidity across the interest rate swap tenor curve is highly concentrated at certain specific points as demonstrated by available data and analysis:

- The AMG has reviewed approximately eleven weeks of SDR execution data for September 1 through November 18, 2013. We found that seven specific tenors in interest rate swaps (one, two, three, five, 10, 20, and 30 year tenors) accounted for 77% of the trade count. The data reviewed by the AMG is consistent with data considered by others.
- In response to another SEF's MAT determination, the Managed Funds Association ("MFA") reviewed interest rate swap data from DTCC's real-time dissemination dashboard.<sup>46</sup> In the six-and-a-half weeks of data MFA reviewed, from October 2 through November 15, there were 11,831 new, cleared, spot-starting, USD fixed-to-floating swaps executed on SEFs or DCMs. 88% of the trades were in "Benchmark Swaps," (*i.e.* one-, two-, three-, five-, seven-, 10-, 15-, 20-, and 30-year tenors), and a further 11.7% were in other "whole" or integer year tenor "non-Benchmark Swaps." MFA found that only 0.3%, or 37 of these swaps, were "Partial Tenor Swaps," *i.e.* non-integer year tenor swaps (for example, a 293 day tenor or a 13 year and 76 day tenor swap).<sup>47</sup>
- According to a 2012 Federal Reserve Bank of New York ("FRBNY") staff report, "[interest rate derivatives] activity in major currencies and products is clustered around a select group of instruments[.]"<sup>48</sup> The report indicated that 64% of US dollar interest rate swaps were in five specific tenors: two; three; five; ten; and 30 years.

In contrast to data reviewed by the AMG, MFA, and FRBNY showing trading activity concentrated in a handful of specific standard tenors, the October MAT Determination groups together these five to 31 liquid, standard tenor swaps with 11,284+ other, less liquid tenor swaps in each of the Three Categories. The October MAT Determination then considers the Three Categories as a whole, attributes liquidity to all of the swaps in each category, and uses this as a basis to assert that each of the more than 11,315 swaps included in the October MAT Determination should be made "available to trade." Because it fails to distinguish between liquid and illiquid swaps within the Three Categories, this approach to grouping together swaps makes it impossible to sufficiently address any of the six MAT Factors for all swaps, particularly

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<sup>46</sup> Managed Funds Association, RE: Industry Filings IF 13-004, 13-005, and 13-007, Nov. 21, 2013, at 6.

<sup>47</sup> *Id.*

<sup>48</sup> Federal Reserve Bank of New York, An Analysis of OTC Interest Rate Derivatives Transactions: Implications for Public Reporting, Staff Report No. 557, Fleming, Jackson, et. al., at 14 (Mar. 2012, revised Oct. 2012), available at [http://www.newyorkfed.org/research/staff\\_reports/sr557.pdf](http://www.newyorkfed.org/research/staff_reports/sr557.pdf).

the illiquid swaps, in the October MAT Determination, as required by Commission regulation 37.10(b).

(c) The October MAT Determination fails to properly consider each of the MAT Factors

The discussion of the six MAT Factors in the October MAT Determination falls well short of demonstrating that all of the swaps contained therein, particularly those with non-standard tenors,<sup>49</sup> have sufficient trading activity to support a MAT determination and a move to a centralized trading environment for such swaps.<sup>50</sup> We present below an assessment of the October MAT Determination's consideration of each of the applicable MAT Factors.

*Ready and willing buyers and sellers* (factor 1)

In the October MAT determination, Javelin presents a list of willing buyer and seller swap dealers for each of the Three Categories, citing "dealers" and the "CFTC" as sources.<sup>51</sup> Yet, the October MAT Determination fails to present information demonstrating which swap dealers would be buyers and sellers in non-standard tenors within the Three Categories.

Moreover, even if Javelin did show that there are potential buyers and sellers acting as dealers in non-standard tenors, this would only demonstrate that there is *potential dealing activity* in such swaps. This is different than demonstrating that there is *actual trading activity* in such swaps. We believe that indicating potential dealing activity is insufficient to demonstrate trading activity or to support a move to a "centralized trading environment."

*Frequency, size of transactions, and trade volume* (factors 2 and 3)

The October MAT Determination presents frequency, size of transactions, and trade volumes in the Three Categories, further sub-divided into three tenor groups: zero to five years, five to 10 years, and 10 to 31 years.<sup>52</sup> The resulting nine currency and tenor groupings include within them liquid and illiquid swaps and are not sufficiently granular to determine whether specific swaps or groups of swaps within each category have any trading activity.<sup>53</sup> The October MAT Determination also fails to present data that is publicly available regarding frequencies, size of transactions, and trade volumes for non-standard tenor interest rate swaps within each of these nine currency and tenor groupings. As discussed above, AMG and others have examined available data, and have found that trading activity is highly concentrated in a small number, less than 0.3%, of the 11,315+ tenors covered by the October MAT Determination.

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<sup>49</sup> *I.e.* non-integer year tenors.

<sup>50</sup> 78 Fed. Reg. at 33,613.

<sup>51</sup> October MAT Determination, at 7.

<sup>52</sup> *Id.* at 8-10. "Javelin asserts that the swaps market is one of the largest and most liquid globally when volume, trade count and average trade size is considered." *Id.* at 10. While it may be true that swap markets are liquid, it does not follow that all swaps are liquid.

<sup>53</sup> 78 Fed. Reg. at 33,612.

*Number and types of market participants (factor 4)*

The October MAT Determination provides a high-level discussion of who might trade interest rate swaps generally.<sup>54</sup> Javelin notes that swap dealers, electronic trading firms, commercial banks, GSEs/mortgage servicers/originators, hedge funds, asset managers, insurance companies, pension funds, REITs, and corporate treasurers/municipalities may use interest rate swaps.<sup>55</sup> Javelin does not, however, consider or present any information on who might trade in non-standard tenors. Nor does Javelin consider or present any information available to it that might indicate the degree of liquidity that these generic categories of market participants would provide for swaps with non-standard tenors included within the October MAT Determination. Frankly, the general information Javelin provides in the October MAT Determination regarding the number and types of market participants could have been submitted for any interest rate swap, liquid or illiquid, whether subject to a clearing requirement or not. The October MAT Determination therefore fails to demonstrate the existence of trading activity or ability to provide a centralized trading environment for any of the swaps included therein.

*Bid/ask spread (factor 5)*

The October MAT Determination presents bid/offer spread data, but only for 13 standard tenors or less than 0.12% of the 11,315+ tenors covered therein.<sup>56</sup> The October MAT Determination fails to consider non-standard tenor interest rate swaps entirely, let alone consider publicly-available information relevant to considering whether such non-standard tenor interest rate swaps have trading activity sufficient to support a MAT determination.<sup>57</sup>

*Usual number of resting firm or indicative bids and offers (factor 6)*

Again, in discussing the usual number of resting firm or indicative bids and offers, the October MAT Determination only provides bid and offer data for 12 standard tenors or less than 0.11% of the swaps included therein.<sup>58</sup> The October MAT Determination therefore does not demonstrate any trading activity within 11,303 of 11,315 (99.89%) tenors covered therein. Nor does Javelin consider publicly-available information that could bear on determining the degree of liquidity in these 11,303 tenors in the October MAT Determination. We do not believe, based on our observations and those of others who have considered the issue (as described above), that there is currently an active trading market with resting firm bids and offers for non-standard tenor swaps.

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<sup>54</sup> October MAT Determination, at 15-17.

<sup>55</sup> *Id.* at 16-17.

<sup>56</sup> *Id.* at 11-13.

<sup>57</sup> *Id.* at 10.

<sup>58</sup> *Id.*

#### **IV. No MAT Determination should extend to “spreads,” packaged, or compound interest rate products at this time**

The October MAT Determination includes “Spreads.”<sup>59</sup> It defines a “spread” as a “combination of interest rate swaps and U.S. Treasury Bonds purchases or sales.”<sup>60</sup> The October MAT Determination does not even mention other packaged or compound interest rate products with swap components (*e.g.*, exchanges for related positions (“EFRPs”), butterflies, curves, invoice spreads, etc.) that another SEF considered in its MAT determination and ultimately chose not to make “available to trade.”<sup>61</sup> These products are not addressed specifically or even in general terms in the October MAT Determination’s consideration of the MAT Factors.

We note that Javelin’s November MAT Determination specifically excludes “Invoice Spreads” and other packaged or compound products, but still includes “USD Spot Starting Benchmark Spreads (versus US Treasuries): 2, 3, 5, 7, 10, 30 years.” The AMG urges the Commission not to permit any “spreads” and other packaged or compound interest rate products within the scope of a MAT determination at this time as no SEF has demonstrated that these products are appropriate for the trade execution requirement.

#### **Conclusion**

We believe that the October MAT Determination fails to demonstrate Javelin’s ability to support “Order Book” trading in most of the swaps in the determination, as required by Commission rules. The October MAT Determination also fails to make the requisite showing of any of the six MAT Factors for the swaps included therein. We believe that it is contrary to the CEA and Commission regulations for a MAT determination to present an “analysis and application” of the MAT Factors that, like the “analysis and application” in the October MAT Determination, is supported only by favorable information and data that is parsed to create an impression of trading liquidity where, in actuality, there is very little. Indeed, one of the purposes of the comment period provided by the Commission for MAT determinations is to provide the public the opportunity to challenge the analysis and information contained therein. As presented above, we believe most of the swaps in the October MAT Determination

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<sup>59</sup> *Id.* at 4.

<sup>60</sup> *Id.*

<sup>61</sup> TrueEx Made Available to Trade Submission of Certain Interest Rate Swaps pursuant to CFTC Regulation 40.6 (Submission 2013-14) (Oct. 21, 2013), at 6 (“There is not sufficient evidence to support that there is the same or similar liquidity when a MAT [interest rate swap] is traded as part of a strategy (*e.g.*, if one or all legs of a switch or butterfly are MAT, or as part of a treasury spread or invoice spread) or as part of a portfolio (*e.g.* one or more line items of a package of positions to be terminated or compacted). For example, a strategy trade would never be considered MAT, even if the combination consisted of MAT x MAT, MAT x MAT x not MAT, etc. nor would a portfolio of transactions in which one or more line items (but not all) are MAT Contracts. This is particularly relevant in the context of CFTC requirements regarding the minimum number of participants to whom a market participant must transmit a request for quote (“RFQ”) and other more stringent requirements for Required Transactions.”).

(especially those with non-standard tenors) lack the requisite trading liquidity under Commission regulation 37.10(b) to be subject to the trade execution requirement.

Although we have not yet thoroughly reviewed the November MAT Determination, based on our initial review, we think it is a considerable improvement and are generally supportive of the changes made by Javelin.<sup>62</sup> We believe that Javelin could have avoided submitting multiple MAT determinations if it had consulted with market participants to determine the appropriate scope together at the outset, as contemplated by Commission regulation 40.6(a)(7)(vi)<sup>63</sup> and by the rulemaking establishing the process to make a “swap available to trade.”<sup>64</sup> We therefore encourage the Commission to promote dialogue between SEFs, DCMs, and market participants before MAT determinations are submitted to the Commission in order to ensure the appropriate scope of these determinations and to conserve Commission resources.

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<sup>62</sup> Nevertheless, we believe that Javelin’s MAT determination could have been streamlined further as the November MAT Determination appears to have retained some of the analysis from the October MAT Determination that should no longer be necessary. In addition, as previously indicated, we do not believe that “USD Spot Starting Benchmark Spreads (versus US Treasuries)” should be in scope for a MAT determination at this time. We reserve the right to make further comments on Javelin’s November MAT Determination based on a more complete review of the amended filing.

<sup>63</sup> A rule submission shall include “brief explanation of any substantive opposing views expressed to the registered entity by governing board or committee members, members of the entity or market participants, that were not incorporated into the rule, or a statement that no such opposing views were expressed.” 17 CFR 40.6(a)(7)(vi).

<sup>64</sup> Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act, 78 Fed. Reg. 33,606, 33,624 (“Relying on SEFs and DCMs [to make MAT determinations], who would be incentivized to make swaps available to trade, to initiate the determination process *in consultation with market participants* will also facilitate innovation and promote swaps trading ...”) (emphasis added) (June 4, 2013).

Commodity Futures Trading Commission

December 2, 2013

We appreciate your consideration of our comments and requests in this letter. We stand ready to provide any additional information or assistance that the Commission might find useful. Should you have any questions, please do not hesitate to contact Tim Cameron or Matt Nevins of AMG at 212-313-1389 or 212-313-1176 respectively or Salman Banaei or Michael Loesch of Norton Rose Fulbright at 202-662-0287 or 202-662-4552 respectively.

Sincerely,



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Timothy W. Cameron, Esq.  
Managing Director, Asset Management Group  
Securities Industry and Financial Markets Association



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Matthew J. Nevins, Esq.  
Managing Director and Associate General Counsel, Asset Management Group  
Securities Industry and Financial Markets Association

cc: Hon. Gary Gensler, Chairman, Commodity Futures Trading Commission  
Hon. Bart Chilton, Commissioner, Commodity Futures Trading Commission  
Hon. Scott O'Malia, Commissioner, Commodity Futures Trading Commission  
Hon. Mark Wetjen, Commissioner, Commodity Futures Trading Commission  
Vincent McGonagle, Director, Division of Market Oversight, Commodity Futures  
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