

WELLINGTON MANAGEMENT COMPANY LLP

280 Congress Street, Boston, Massachusetts 02210 USA

T +1 617.951.5000
www.wellington.com

WELLINGTON
MANAGEMENT®

Via CFTC Comments Portal (<https://comments.cftc.gov>)

15 March 2019

Mr. Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

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

Dear Mr. Kirkpatrick,

Wellington Management Company LLP (**Wellington**) appreciates the Commission's prior work to promulgate rules for swaps execution facilities (**SEFs**) as well as its ongoing assessment of these rules through the Commission's 2018 Release.¹ Wellington uses swaps among other instruments to manage investments for mutual funds, pension funds, private funds and other investors seeking returns through active management of portfolios. Wellington believes that the Commission's current SEF regulations work well and have fostered electronic markets with demonstrated improvements to liquidity and pricing for our clients. Nonetheless, Wellington agrees that targeted changes to SEF regulations would advance the objectives of Dodd-Frank and further improve these electronic markets. Among these changes, we support revising the trade execution requirement so that swaps meeting minimum standards of client-traded volume and technological connectivity for client transactions are mandated for trading on SEFs. We believe a SEF should evidence satisfaction of these criteria and initiate a public comment period prior to submitting its request for a trade execution requirement with the Commission. With these and other enhancements discussed below, Wellington believes that the current SEF environment will continue to improve.

Specifically, we provide the following views on the 2018 Release:

Wellington supports the Commission's proposed definition of the term "market participant" as it would no longer include clients who do not execute or direct activity on a SEF. The Commission's revision of the definition of market participant, which narrows the scope to persons who execute or direct activity on a SEF,² resolves prior issues for our clients who are not themselves making trading decisions when we trade on their behalf. We support the Commission's effort to clarify this term and urge the Commission to adopt the proposed definition.

¹ Swap Execution Facilities and Trade Execution Requirement, 83 Fed. Reg. 61,946 (Nov. 30, 2018) (the **2018 Release**).

² See 2018 Release, Proposed Regulation 37.2(b) (proposing to define "market participant" to mean any person who accesses a SEF through: (i) direct access provided by a SEF; (ii) indirect access or functionality provided by a third-party; or (iii) directing an intermediary that accesses a SEF on behalf of such person to trade on its behalf).

Wellington supports maintaining the Commission’s current interpretation of impartial access. We do not believe that the Commodity Exchange Act (CEA), including Section 5h(f)(2)(B),³ permits SEFs to discriminate between different categories of market participants in access to trading. If the Commission were to approve outright or de facto discrimination of market participants from executing, viewing pricing data screens, or using particular methods of execution, our clients would likely experience inferior pricing on SEFs. Given this negative consequence, we disagree with the 2018 Release’s suggestions to allow interdealer SEFs or other forms of differentiation among market participants.⁴ Rather than move more towards a two-tiered market, we recommend codifying Commission Staff’s 2013 interpretation of impartial access and holding SEFs to these standards.⁵

While Wellington supports changing SEF regulations to allow more flexible modes of execution, we believe the Commission should review new modes as they are proposed by SEFs to assess whether they meet the CEA’s requirement to “provide market participants with impartial access,” and balance the CEA’s goals of “promot[ing] the trading of swaps” on SEFs and “pre-trade price transparency.”⁶ While we currently use request-for-quote-to-three (RFQ-3) and find that this mode of execution works well for swaps with sufficient electronically traded client volume and technological connectivity, we do not believe that RFQ-3 and order books are the only execution methods that promote central execution and pre-trade price transparency while allowing impartial access. As more swaps trade on SEFs, we would like to see innovation guided by these criteria and believe Commission Regulation 37.9 could impede progress. In addition, we support development of liquidity in order books through, among other things, technological development of average pricing by clearing members and SEFs.

Wellington believes that the trading mandate should only include swaps that meet a specified threshold of client-traded volume supported by technology for multiple types of client order submissions. Our experience with voluntary execution of swaps demonstrates to us that an on-SEF execution requirement cannot be co-extensive with a clearing mandate. Wellington typically clears swaps voluntarily when liquidity has developed, and then considers whether and how we can trade those swaps electronically. Not all swaps that we voluntarily clear can also be executed electronically due to lack of on-SEF trading volume. In addition, some contracts have non-standard attributes that must be addressed prior to executing electronically. For example, each new currency in which swaps are denominated (*e.g.*, emerging market currencies) has its own nuances on the terms and conditions that require technical development and conformance testing with the SEFs.

We recommend the following process to mandate a swap for trading on-SEF:

- (1) **SEF publishes a proposal for public comment regarding the trading mandate.** The proposal should include evidence that: (a) on-SEF client trading exceeds a specified volume for a specified period of time predetermined by the Commission; and (b) the SEF has existing automated capability to support client orders,

³ CEA § 5h(f)(2) (“A swap execution facility shall ... (B) establish and enforce trading, trade processing, and participation rules that will deter abuses and have the capacity to detect, investigate, and enforce those rules, including means—(i) to provide market participants with impartial access to the market.”).

⁴ *See, e.g.*, 2018 Release at 61995 (“... a SEF could premise these criteria in different ways, such as limiting access upon the type of the market participant or the swap product itself. For example, a SEF would be able to calibrate access to serve market participants within a particular market segment, such as dealers trading in a wholesale swaps market, who may be categorized as ‘similarly situated.’”).

⁵ *See* Division of Clearing and Risk, Division of Market Oversight and Division of Swap Dealer and Intermediary Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities (Nov. 14, 2013), *available at*, <https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/dmostaffguidance111413.pdf>.

⁶ CEA § 5h(e) (“The goal of this section is to promote the trading of swaps on swap execution facilities and to promote pre-trade price transparency in the swaps market.”).

including straight-through processing to the FCMs and CCPs. We recommend that the public comment period be open for at least 45 days.

- (2) **SEF submits request for trading mandate to the Commission.** If the SEF receives no material objections to the proposal, the SEF could file for self-certification under Commission Regulation 40.6. If, however, the proposal receives comments raising material concerns or objections, the submission should be deemed “novel or complex” within the meaning of Section 5c(c)(2) of the Act, and automatically subject to public comment by the Commission pursuant to Section 5c(c)(3) of the Act. This process would not only allow for consideration of whether the mandate is consistent with the CEA but also afford the Commission an opportunity to assess whether the SEF’s filing met all applicable criteria for submission. If, for example, the submission lacked sufficient evidence of on-SEF client trading volume or technological readiness, or if the SEF does not sufficiently resolve objections raised during its comment period, the Commission could reject the submission as improperly filed.
- (3) **Upon self-certification or determination to mandate trading of a swap on SEF, the process should provide a minimum period of 90 days before the new trading mandate becomes effective to allow sufficient time to build out and test any additional requirements.**

Wellington believes that the Commission should continue to allow negotiation of block trades off-SEF. The Commission should continue to permit market participants to engage in off-SEF negotiation of block trades so that market participants can appropriately price these large trades and reduce risks of information leakage. We further support continuing to allow block trades to be booked via SEF to facilitate compliance with other requirements, such as pre-trade credit checks, clearing and regulatory reporting. If the Commission is concerned about the market percentage comprised of block trades, we suggest that the Commission propose changes to reset the block trade thresholds based on its analysis of market data.

Wellington agrees with the 2018 Release’s suggestion to allow package transactions to be negotiated off-SEF and excluded from the trade execution requirement when only one leg of the package is subject to a mandatory trading determination.⁷ Much like block transactions, package transactions need to be negotiated off-SEF unless the package as a whole satisfies the standards for mandating execution on-SEF.

Wellington believes that the Commission should continue to allow pre-trade communication of client-dealer market color and trade ideas to occur off-SEF.

Wellington agrees with the 2018 Release’s trade error policy of void *ab initio* for errors other than administrative or clerical ones;⁸ however, we believe that the administrative or operational errors exception should be expanded to include credit-related rejections due to administrative or operational errors or intraday limit adjustments subject to the discretion of the FCM. We believe the Commission’s proposed approach is helpful to enable counterparties to continue trading without need for breakage agreements to cover on-SEF trading. We have found, however, that some credit-related rejections are due to system failures, other operational reasons (i.e. new client account not fully setup) or the need to move limits between categories (i.e. credit vs. rates) and believe those types of failures should be addressed by allowing resubmission of the trade for clearing.

* * * *

⁷ 2018 Release at 61987.

⁸ 2018 Release at 62065.

CFTC – SEF and Trade Execution Requirement
15 March 2019

We appreciate the Commission's consideration of our comments. Should you have any questions, please contact Laura Martin or me at the number above.

Respectfully submitted,



Anne P. Colucci, CFA
Associate Director, Global Trading