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VIA ELECTRONIC DELIVERY

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: COMMENTS ON THE PROPOSED RULE, SWAP EXECUTION FACILITIES AND TRADE EXECUTION REQUIREMENT (RIN 3038-AE25)

Dear Secretary Kirkpatrick:

I. INTRODUCTION.

Munich Re Trading LLC (“**MRTL**”) respectfully submits this letter in response to the request for public comment set forth in the Commodity Futures Trading Commission’s (the “**Commission**” or “**CFTC**”) Proposed Rule, *Swap Execution Facilities and Trade Execution Requirement* (the “**SEF Proposed Rule**”).¹ MRTL is a Delaware limited liability company and a wholly-owned subsidiary of Münchener Rückversicherungs-Gesellschaft (“**MRAG**”). MRTL is a *de minimis* swap dealer and natural gas marketing company with its principal place of business in The Woodlands, Texas.

MRTL acts as a swap intermediary in markets for weather derivatives and energy commodities. MRTL is one of the largest weather derivatives dealers in North American swap markets. In addition to the foregoing, MRTL also currently provides natural gas marketing and fuel procurement services.

MRTL appreciates the Commission’s ongoing efforts to strengthen the swaps regulatory framework implemented pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 through the reduction of unnecessary complexity, costs, and other burdens that impede market development, innovation, and growth. MRTL supports the Commission’s efforts to maintain a transparent and open dialogue with market participants and stakeholders with respect to its regulatory agenda and policy priorities.

In this respect, MRTL broadly supports the Commission’s efforts to rethink certain aspects of the regulation of swap execution facilities (“**SEFs**”) and the related trade execution requirement. Through these comments, MRTL seeks to address a relatively narrow, but important, issue with respect to the application of the SEF registration requirement to certain swaps brokering entities. As discussed in Section II. below, MRTL respectfully requests that the Commission limit the scope and application of the proposed SEF registration requirements in order to minimize potential disruption in certain highly specialized and thinly traded pockets of commodity derivative markets that rely on the expertise and services of small, independent introducing brokers (“**Small IBs**”).

¹ *Proposed Rule, Swap Execution Facilities and Trade Execution Requirement*, 83 Fed. Reg. 61,946 (Nov. 30, 2018), <https://www.cftc.gov/sites/default/files/2018-11/2018-24642a.pdf>.

II. COMMENTS OF MRTL.

A. **Overly Broad SEF Registration Will Negatively Affect Smaller, Highly Specialized, and Thinly Traded Markets.**

As a *de minimis* swap dealer, MRTL focuses its business on serving customers in weather derivatives markets and certain niche aspects of energy commodity markets. These markets are characterized by their small size, periodic transaction activity, and highly specialized nature. As a small business of approximately 32 full-time employees, MRTL has only three originators on staff. These originators are limited in the scope of territory and number of customer relationships they can individually cover. Given these constraints, MRTL routinely relies on the services of Small IBs whose expertise and customer relationships are critical to bringing liquidity and facilitating price discovery in these markets.

Many of the Small IBs with whom MRTL does business are sole proprietorships or small businesses (*i.e.*, two to six employees). These Small IBs are all standalone voice brokers as, to the best of MRTL's knowledge, none of the Small IBs that MRTL works with own, operate or utilize electronic platforms or systems designed to facilitate the higher volumes of transaction activity that the SEF Proposed Rule associates with "many-to-many" swaps trading. Rather, the business model for such Small IBs is generally "one-to-many" and is predicated on soliciting an order from a market participant and introducing that order to swap counterparties. In this respect, the total amount of brokered transactions – both in terms of number of transactions executed and notional value of such transactions – is *de minimis* when compared to the volumes handled by large swaps brokering entities, such as the interdealer brokers operating in interest rate swap and credit default swap markets.

The following example illustrates MRTL's reliance on Small IBs to help end-users hedge odd-lot exposure to price risk in U.S. heating oil markets:

Heating oil is typically sold by distributors to retail consumers at a fixed-price. In the Northeastern U.S., a retail consumer typically will use approximately 750 gallons of fuel oil over the duration of a winter season. As soon as the distributor sells the first gallon of heating oil to a retail consumer, it incurs price risk.

Given the small size of this exposure, the distributor is unable to hedge this position outright in futures markets. The contract unit size for a single NYMEX NY Harbor ULSD futures (HO) contract is 42,000 gallons. As such, to hedge using a single NYMEX HO futures contract, the distributor must wait until it has sold the equivalent of 170 tanks of heating oil. Rather than hold this risk on its books until (and if) its aggregated exposures can be hedged as a single position in the NYMEX HO futures market, the distributor will work with a Small IB to mitigate its current risk exposure with a swap counterparty.

The Small IB will facilitate a swap with a counterparty like MRTL that is willing to enter into a swap that meets the distributor's odd-lot risk exposure. MRTL may also provide the distributor an instrument to hedge the weather-related portion of its risk (e.g., a longer or colder than expected winter). MRTL then warehouses and aggregates its odd-lot heating oil exposures until it has positions large enough to hedge using the NYMEX HO futures contract and retains the weather risk on its balance sheet.

Large financial institutions and swaps brokering entities do not compete for such odd-lot business due to the prohibitive cost of doing business given the small and specialized nature of these swap markets. If the Small IBs servicing this market were forced out of business due to burdens and costs imposed by SEF registration, heating oil distributors would be unable to hedge and would be required to sell at a floating, rather than a fixed, price. This would result in homeowners, as well as corporate and industrial customers, having direct exposure to heating oil price risk. MRTL provides such odd-lot business in order to obtain access to the weather risk business, which is core to its business model and which is risk that MRAG views as diversifying to its overall global portfolio.

MRTL is concerned that the application of the SEF registration requirement to Small IBs would impose compliance costs and burdens that these entities do not have the financial wherewithal to bear and, thus, force them out of business. The loss of Small IBs would be detrimental not only to orderly

operation and trading in these small, highly specialized markets, in this example it would increase the exposure to heating oil price risk of end-users who rely on their services. Such increased risk exposure would ultimately be borne by consumers in the form of higher commodity prices. The loss of Small IBs also would stifle innovation critical to the development of new and efficient risk management products offered in these markets (such as allowing the heating oil distributor to hedge the weather-related portion of its risk in the above example).

Structurally, the potential loss of Small IBs in such specialized markets would create a void that likely could only be filled by large financial institutions/swaps brokering entities. To date, these larger players have been content with Small IBs meeting customer demand, as the cost of market entry (including the need to hire and develop internal market expertise) taken together with smaller-scaled and limited transaction activity has acted as a deterrent to their participation. If Small IBs were forced out of business due to the costs and burdens of SEF registration, it is not clear whether large financial institutions/swaps brokering entities would enter the market. However, if they do, MRTL is concerned that this would likely result in a market environment where swaps pricing is less competitive due to the (i) increased dominance of these larger players, and (ii) their need to charge what would historically be viewed as “out-of-market” premiums to simply cover their increased costs and limited economic upside.

The SEF Proposed Rule recognizes the potential adverse impacts that an expanded SEF registration requirement would have on Small IBs, including the market participants that rely upon these entities, such as MRTL. Specifically, the SEF Proposed Rule notes the following:

Smaller entities or platforms are less likely to have existing technology and procedures or available resources to comply with new SEF requirements; therefore, their initial costs of compliance with those requirements may be larger or have a proportionally greater effect on smaller entities. Market participants may also bear some costs if some entities abstain from SEF activities. For example, market participants who have utilized these entities to trade swaps would no longer be able to do so for swaps that must be traded on a SEF or swaps that they would otherwise want to execute on a SEF. Therefore, these participants would incur costs that could include search and transition costs to identify and onboard to new SEFs. In transitioning to a new platform, those market participants may incur less favorable financial terms or have access to reduced services.²

For the reasons described herein, MRTL respectfully requests that the SEF registration requirements adopted in any final rule issued in this proceeding be appropriately tailored in their scope and application to avoid potential disruption to smaller, highly specialized commodity markets, such as those for weather derivatives and certain aspects of energy commodity markets. Apart from legal arguments addressed in Section II.B., below, strong public policy grounds exist for protecting the integrity of such markets by ensuring that Small IBs are not precluded from being able to provide their expertise, bring liquidity and facilitate price discovery therein.

B. As Proposed, SEF Registration Would Categorically Apply to all Swaps Brokers.

The legal underpinnings of MRTL’s concerns raised in Section II.A. are as follows. As contemplated by the SEF Proposed Rule, SEF registration would essentially apply to all swaps brokering entities, whether large or small.³ This expansive application of the SEF registration requirement is based on the Commission’s proposed interpretation that the activities of such entities, including standalone voice brokers “allow multiple participants to *trade* swaps with multiple participants....(emphasis added).”⁴ In this respect, the Commission takes the position that “it is necessary to apply the SEF registration requirement to ensure that the multiple-to-multiple ‘trading’ that occurs on such trading systems or platforms is subject to the [CEA] and [CFTC]’s regulations as regulated SEFs,” and that

² SEF Proposed Rule at 62,054.

³ See Proposed Rule at 61,957 (proposing to apply the SEF registration requirement to swaps brokering entities, including interdealer brokers). Large and small swap introducing brokers entities are collectively referred to herein as “**Swaps Brokers**.”

⁴ Proposed Rule at 61,957.

“[t]his application is consistent with Congressional intent, as evidenced by the statutory SEF registration requirement and SEF definition, and is further consistent with the statutory SEF goals.” MRTL disagrees with this premise. Specifically, standalone voice brokers’ typical tools of communication with their customers: email, instant message, phone, and voice box, do not constitute a “trading system” or “platform” for the purposes of the definition of SEF in the CEA.⁵ As such, MRTL strongly urges the Commission not to adopt a final rule in this proceeding that would categorically apply SEF registration to all Swaps Brokers, especially standalone voice brokers.

The categorical application of the SEF registration requirement to Swaps Brokers is inconsistent with the CEA and Congressional intent underlying the Dodd-Frank Act, as it effectively nullifies and renders moot the requirement in the CEA for Swaps Brokers themselves, as well as for associated persons of Swaps Brokers, to register with the Commission and National Futures Association. When enacting the Dodd-Frank Act, Congress clearly intended Swaps Brokers and SEFs as separate concepts and to function as distinct types of legal entities. This intent is reflected by Congress’ inclusion of the term “swap” in the definition of “introducing broker”⁶ while it also added a separate definition of “swap execution facility” to the CEA. Not only does the SEF Proposed Rule’s potential categorical treatment of Swaps Brokers as SEFs conflict with Congressional intent, it is also contrary to a fundamental maxim of statutory construction, which is that every clause and word of a statute should be given effect, if possible, and entire sections should not be read out.⁷ The categorical application of SEF registration to Swaps Brokers defies this maxim by reading the term “swap” out of the statutory definition of “introducing broker,” as set forth in CEA Section 1a(31).

C. Proposals for Implementing an Appropriately Tailored SEF Registration Requirement.

If it is ultimately the Commission’s determination that it is appropriate to issue a final rule in this proceeding implementing the SEF registration requirement in a form similar to the SEF Proposed Rule, MRTL urges the Commission to consider options that would minimize the potential disruption to smaller, highly specialized and thinly traded commodity derivative markets. Specifically, MRTL suggests that the Commission adopt a *de minimis* exception to the SEF definition and related registration requirements.⁸ Prior to adopting an exception, the Commission should review the data available to it and propose a number of potential alternative approaches to the exception as part of any additional proposal or final rule issued with respect to the definition of SEF. MRTL welcomes the opportunity to further engage with the Commission and, as needed, function as outside resource for purposes of working to develop a *de minimis* exception that concurrently recognizes the policy objectives underlying SEF market design and avoids potential disruptive impacts on small, highly specialized and thinly traded markets.

⁵ CEA Section 1a(50) defines the term “swap execution facility” to mean

“A trading system or platform in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility, that—

- (A) facilitates the execution of swaps between persons; and
- (B) is not a designated contract market.”

⁶ Under CEA Section 1a(31), the definition of an “introducing broker” includes any person who:

- “is engaged in soliciting or in accepting orders for— the purchase or sale of any commodity for future delivery, security futures product, or swap...;” and
- “does not accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom.”

⁷ See *United States v. Menasche*, 348 U.S. 528, 538–39 (1955).

⁸ A *de minimis* exception from the SEF definition and related registration requirements could be structured in a number of ways to avoid the potential for abuse. For example, it could be limited to certain classes of derivatives, such as commodity derivatives, and could be based on any number of factors, such as the size of the swaps brokering entity itself (*i.e.*, number of employees (Principles and Associated Persons)), transaction size, transaction count, trading frequency, or notional volume.

III. CONCLUSION.

MRTL appreciates this opportunity to provide input on the SEF Proposed Rule and respectfully requests that the comments set forth herein are considered.

If you have any questions, please contact the undersigned.

Sincerely,

/s/ Mark Tawney _____
Mark Tawney, President
Munich Re Trading LLC

/s/ JannaLyn Allen _____
JannaLyn Allen, General Counsel
Munich Re Trading LLC