

May 20, 2020

Christopher Kirkpatrick, Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, NW  
Washington, D.C. 20581

Re: CFTC Request for Comment on Proposal on Real-Time Public Reporting Requirements, RIN 3038—AE60

Dear Mr. Kirkpatrick:

We appreciate the opportunity to provide feedback and comment regarding the CFTC’s proposed revisions to its regulations on real-time public reporting requirements. The Commission’s proposal would permit a time delay of 48 hours for disseminating price data for swap transactions above a specified block size. This delay is a significant change in the reporting regime for large swap transactions. Evaluating the delay is an important issue in the CFTC’s assessment of the rule-making.

By way of background, the three authors of this comment letter are currently studying the impact of dissemination caps and the intermediation process more broadly in the corporate bond market and previously analyzed the impact of dealer trading networks for structured products on trading costs and price discovery.<sup>1</sup> Burton Hollifield also has extensively studied the market design of the municipal bond market and the impact of price opacity.<sup>2</sup> Chester Spatt served as Chief Economist of the Securities and Exchange Commission (2004-2007) during the adoption and implementation of Regulation NMS (National Market System) and served as a member of the SEC’s Equity Market Structure Advisory Committee (EMSAC) from 2015 through 2017.<sup>3</sup> Both Hollifield and Spatt also have examined in separate studies a range of regulatory and market design issues involving the equity markets.

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<sup>1</sup> A. Neklyudov, B. Hollifield and C. Spatt, 2020, “Volume and Intermediation in Corporate Bond Markets,” unpublished manuscript and A. Neklyudov, B. Hollifield and C. Spatt, 2017, “Bid-Ask Spreads, Trading Networks, and the Pricing of Securitizations,” *Review of Financial Studies* 30, 3048-3085.

<sup>2</sup> R. Green, B. Hollifield and N. Schurhoff, 2006, “Financial Intermediation and the Costs of Trading in an Opaque Market,” *Review of Financial Studies* 20, 275-314 and R. Green, B. Hollifield and N. Schurhoff, 2007, “Dealer Intermediation and Price Behavior in the Aftermarket for New Bonds,” *Journal of Financial Economics* 86, 643-682.

<sup>3</sup> Spatt was one of the founders in the mid-1980s of the *Review of Financial Studies* (which quickly emerged as among the three leading journals in finance) and its second executive editor and served as President of both the Society for Financial Society and the Western Finance Association. Besides the EMSAC, he also has served as a member of both the Model Validation Council of the Federal Reserve System and the Advisory Committee of the Office of Financial Research as well as various non-governmental groups, such as the Systemic Risk Council, the Shadow Financial Regulatory Committee and the Financial Economists Roundtable.

The three authors of this letter previously commented on a related proposal by FINRA to examine a proposed pilot program on corporate bond block trade dissemination.<sup>4</sup> The proposed FINRA rule-making would examine a 48-hour dissemination delay for trading investment-grade corporate bonds above \$ 5 million and for trading high-yield corporate bonds above \$ 1 million. It also would examine an increase in the current dissemination cap from \$ 5 million to \$ 10 million for investment-grade corporate bonds and from \$ 1 million to \$ 5 million for high-yield corporate bonds. The 48-hour delay in transaction price dissemination would be in a similar vein to the CFTC's proposal for the swaps market. Our comment letter was critical of FINRA's proposal to delay price reporting for 48 hours for the larger trades. Indeed, much of the buy-side and end-user investor community was similarly critical of the FINRA proposal, as reflected in an account in the *Wall Street Journal* a few weeks after the close of the comment period and a more recent account in *Bloomberg*.<sup>5</sup> We were surprised that the CFTC's filing for the proposal for which we are commenting did not point to the 48-hour delay proposed by FINRA, whose own comment period closed almost one year ago (June 2019). Given that, we feel that it is particularly important to call this to the CFTC's attention in our current letter. Strikingly, the FINRA proposal appears not to be moving forward, as illustrated by a recent media account in *Bloomberg*.<sup>6</sup> The extent of the parallel of the FINRA proposal to the CFTC proposal is striking, as is the lack of follow-up rule-making by FINRA and the absence of discussion and presentation of these realities by the CFTC.

While our recent collective focus has been to study transparency and broader aspects of market structure in various bond markets rather than the swaps market, we feel nevertheless that our findings, analyses and conclusions would be informative for the current CFTC rule-making. It is clear from prior studies that price transparency has reduced the transaction costs of trading in the bond markets. In the presence of dissemination caps currently prevailing in those markets, price reporting still arises, but the reporting of the size of large trades is truncated at the dissemination cap (currently \$5 million for investment-grade instruments and \$ 1 million for high-yield ones). A variety of studies have made clear that price reporting (price transparency) has played an important role in the reduction of the trading costs in fixed-income markets<sup>7</sup> and especially, the costs experienced by smaller investors. As a result, we are skeptical about creating a substantial dissemination delay and opacity for reporting the prices of large transactions, which are central to the price discovery process. Such a delay would significantly disadvantage smaller investors and potentially retard much of the improvement in the quality of the fixed-income market since the

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<sup>4</sup> Our comment letter is available at [https://www.finra.org/sites/default/files/2019-06/19-12\\_Spatt-Hollifield-Neklyudov\\_comment.pdf](https://www.finra.org/sites/default/files/2019-06/19-12_Spatt-Hollifield-Neklyudov_comment.pdf).

<sup>5</sup> M. Wirz, June 27, 2019, "Bond Fight Pits Main Street Against Wall Street," *Wall Street Journal*, <https://www.wsj.com/articles/bond-fight-pits-main-street-against-wall-street-11561633200> and B. Chappatta, "Wall Street's Bond Transparency Letters are Revealing," *Bloomberg*, <https://www.bloomberg.com/opinion/articles/2020-01-22/wall-street-s-bond-transparency-letters-are-revealing?sref=BNAbdgOy> .

<sup>6</sup> B. Bain, "Delayed Disclosure of Biggest Corporate Bond Trades Stall," *Bloomberg*, January 22, 2020, <https://www.bloomberg.com/news/articles/2020-01-22/a-48-hour-delay-for-bond-trades-stalls-after-wall-street-balks?sref=BNAbdgOy> .

<sup>7</sup> See, for example, H. Bessembinder and W. Maxwell, 2008, "Transparency and the Corporate Bond Market," *Journal of Economic Perspectives* 22, 217-234; P. Asquith, T. Covert and P. Pathak, 2013, "The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market, NBER Working Paper No. 19417; and F. Trebbi and K. Xiao, 2019, "Regulation and Market Liquidity," *Management Science* 65, 1949-1968.

introduction of price transparency. While a substantial dissemination delay has reflected the goals of dealers and large buy-size market participants, this has not been accompanied by strong empirical evidence from the markets. Indeed, when one of us served as Chief Economist of the Securities and Exchange Commission, he informally requested to dealers criticizing the move to price transparency in the bond market that they provide studies or evidence to support their critique, but none was forthcoming. In principal, one could argue that the development of an upstairs block market would enhance fixed-income trading, but indeed in the equity arena the emphasis on competition across platforms has resulted in tighter spreads—despite the demise of the upstairs block market for equity.<sup>8</sup>

By way of background we have been studying the impact of current volume dissemination caps in the corporate bond market (A. Neklyudov, B. Hollifield and C. Spatt, 2020, “Volume and Intermediation in Corporate Bond Markets,” unpublished manuscript). In the spirit of regression discontinuity methods, our empirical analysis focuses upon actual trade size slightly above and below the reporting cap. The current level of the dissemination caps does not appear to have much impact on price discovery and the predictability of returns or on customer mark-ups and realized spreads. Our current evidence suggests that volume transparency isn’t very important in the presence of price transparency. In effect, the market infers what it needs to know about volume and potentially obtains information about market color in various ways.

FINRA’s regulatory proposal suggests that an increase in the dissemination cap could offset the reduction in transparency from the substantial delay in dissemination. We disagreed with this perspective based upon our preliminary finding around the cap. We don’t find much evidence that the cap was particularly important in the presence of a robust price reporting regime. In effect, we view volume information as second order for price discovery compared to the basic price reporting (the actual volume above the cap does not add much information in the presence of price information). While increasing the dissemination cap causes volume to be revealed for a broader range of values--that would not seem so important, especially relative to the costs associated with 48-hour delays in price dissemination to the marketplace.

In the FINRA context in the corporate bond market, we pointed to the possibility of a lower dissemination cap; then volume information would be more limited—but without the adverse consequences to the marketplace of not disseminating prices. This could be a natural alternative for protecting dealers compared to a dissemination delay. While the recent focus in our empirical work on reporting caps suggests that there is not a lot of action around the cap, that is arguably a finding around the current level of the dissemination cap, but opacity of the volume could be helpful when the range of potential volumes is broader. In fact, Haoxiang Zhu (an MIT financial economist who is an expert on derivatives markets and market structure) explicitly suggested in his comment letter that the CFTC employ a volume dissemination cap rather than a 48-hour dissemination delay to address similar objectives.<sup>9</sup> As our analysis of the corporate bond proposal and the discussion above suggests, capping the reported size of block transactions could be undertaken without the adverse consequences for trading and resource allocation that would flow from severely restricted price reporting and dissemination.

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<sup>8</sup> See, Section 2.20 in J. Angel, L. Harris and C. Spatt, 2015, “Equity Trading in the 21<sup>st</sup> Century: An Update,” *Quarterly Journal of Finance* 5, 1-39.

<sup>9</sup> [http://www.mit.edu/~zhuh/Comment\\_letter\\_CFTC\\_48h\\_delayed\\_reporting.pdf](http://www.mit.edu/~zhuh/Comment_letter_CFTC_48h_delayed_reporting.pdf).

The FINRA proposal for the corporate bond market included a randomized control trial to evaluate separately and independently in the pilot design the 48-hour dissemination delay and the potential increase in the dissemination cap. We felt that the FINRA proposed pilot has been thoughtfully designed to the extent that one wants to study changes in the dissemination cap (which addresses transparency in the size of trading) and the introduction of a substantial dissemination delay (limiting price transparency for larger transactions). We also felt that the inclusion of a randomized control trial was an important and very helpful dimension to the FINRA proposal, which is absent from the CFTC's own proposal. If the dissemination delay were to be incorporated in the corporate bond market on a long-term basis, then first using a randomized control study along the lines of that proposal would be essential. In contrast, we are struck by the absence of such a randomized control analysis in the CFTC's proposal. Analogously, given the skepticism that we possess about the merits of a 48-hour price dissemination delay for blocks, we do not support efforts to move forward to create such a delay in the absence of a serious randomized control study and strong systematic empirical evidence in support of the proposal.


In summary, though we felt that FINRA's proposed randomized control pilot was well designed, we questioned the need for undertaking such a pilot study to address dissemination delays in light of the widely documented value of price transparency for the bond markets. Our empirical findings based upon the current dissemination caps suggest that these do not have much impact on price discovery or customer costs near the current caps.

While we have not studied empirically the swaps markets directly, we feel that our analysis of the empirics in the corporate bond markets suggests the need for considerable skepticism about the CFTC's rule-making proposing a 48-hour dissemination delay for large blocks. Price transparency has been extremely important in the financial markets. We are deeply concerned about proposed measures to suppress price transparency, especially price transparency on the most important and significant trades. Such block trades are central to the price discovery process and indeed, the 48-hour price reporting delay would undercut price discovery in related instruments. Furthermore, we are struck by the absence of strong support to reduce price transparency in the empirical literature for swaps and derivatives<sup>10</sup> and even the absence of an attempt through the proposal to undertake a careful randomized control trial to support the proposed 48-hour delay on price dissemination, unlike the somewhat parallel proposal from FINRA in the corporate bond context.

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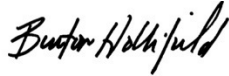
<sup>10</sup>In contrast, support for the value of transparency in the credit default swaps market is provided by Y. Loon and Z. Zhong, 2014, "The Impact of Central Clearing on Counterparty Risk, Liquidity and Trading: Evidence from the Credit Default Swap Market," *Journal of Financial Economics* 112, 91-115 and Y. Loon and Z. Zhong, 2016, "Does Dodd-Frank Affect OTC Transaction Costs and Liquidity? Evidence from Real-Time CDS Trade Reports," *Journal of Financial Economics* 119, 645-672.

Sincerely,



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