

## SWAP EXECUTION FACILITY CLARIFICATION ACT

\_\_\_\_\_

FEBRUARY 8, 2012.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

\_\_\_\_\_

Mr. LUCAS, from the Committee on Agriculture,  
submitted the following

### R E P O R T

together with

### ADDITIONAL VIEWS

[To accompany H.R. 2586]

[Including cost estimate of the Congressional Budget Office]

The Committee on Agriculture, to whom was referred the bill (H.R. 2586) to refine the definition of swap execution facility in the provisions regulating swap markets added by title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike all after the enacting clause and insert the following:

#### SECTION 1. SHORT TITLE.

This Act may be cited as the “Swap Execution Facility Clarification Act”.

#### SEC. 2. DEFINITION OF SWAP EXECUTION FACILITY.

(a) COMMODITY EXCHANGE ACT.—Section 1a(50) of the Commodity Exchange Act (7 U.S.C. 1a(50)) is amended—

(1) by striking “The term” and inserting the following:

“(A) IN GENERAL.—The term”;

(2) by redesignating subparagraphs (A) and (B) as clauses (i) and (ii), respectively, and increasing the indentation of each such provision by 2 ems; and

(3) by adding at the end the following:

“(B) INTERPRETATION.—In interpreting or further defining the term ‘swap execution facility’, the Commission shall not require a swap execution facility to—

“(i) have a minimum number of participants receive a bid or offer or respond to any method of trading functionality;

“(ii) delay bids or offers for any period of time; or

- “(iii) limit the means of interstate commerce utilized by market participants to enter into and execute any swap transactions on the method of trading functionality.”.
- (b) SECURITIES EXCHANGE ACT OF 1934.—Section 3(a)(77) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(77)), as added by section 761(a)(6) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, is amended—
- (1) by striking “The term” and inserting the following:
    - “(A) IN GENERAL.—The term”;
  - (2) by redesignating subparagraphs (A) and (B) as clauses (i) and (ii), respectively, and increasing the indentation of each such provision by 2 ems; and
  - (3) by adding at the end the following:
    - “(B) INTERPRETATION.—In interpreting or further defining the term ‘security-based swap execution facility’, the Commission shall not require a security-based swap execution facility to—
      - “(i) have a minimum number of participants receive a bid or offer or respond to any trading system or platform functionality;
      - “(ii) display or delay bids or offers for any period of time;
      - “(iii) limit the means of interstate commerce utilized by market participants to enter into and execute any security-based swap transactions on the trading system or platform; or
      - “(iv) require bids or offers on one trading system or platform operated by the swap execution facility to interact with bids or offers on another trading system or platform operated by the swap execution facility.”.

#### SEC. 3. IMPLEMENTATION.

The amendments made by this Act shall be implemented—

- (1) without regard to—
  - (A) chapter 35 of title 44, United States Code; and
  - (B) the notice and comment provisions of section 553 of title 5, United States Code; and
- (2) through the promulgation of an interim final rule.

#### BRIEF EXPLANATION

The Dodd-Frank Wall Street Reform and Protection Act (P.L. 111–203) (the Dodd-Frank Act) mandates that all swaps required to be cleared must also be submitted for trading on a regulated exchange or a “swap execution facility” (SEF). While Dodd-Frank provides a statutory definition of SEF, the Commodity Futures Trading Commission (CFTC), and the Securities and Exchange Commission (SEC) with regard to security-based swap execution facilities, are granted authority to further define the term. H.R. 2586 is aimed at clarifying congressional intent with regard to the further definition of SEF by prohibiting the CFTC from: requiring a SEF to have a minimum number of participants receive bids or offers through a Request for Quote system (RFQ), requiring SEFs to delay bids or offers for a specific time period, and limiting the use of any means of interstate commerce to execute swap transactions. There are mirroring provisions placing prohibitions on the SEC’s ability to further define security-based swap execution facilities.

#### PURPOSE AND NEED

Section 1a(50) of the Commodity Exchange Act as amended by Section 721(a)(50) of Dodd-Frank defines a SEF as “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 market participants in the facility or system, through any means of interstate commerce . . .” The CFTC is then given authority to further define the term and establish requirements for SEFs. There is a mirroring provision in Subtitle B of Title VII related to security-based swap execution facilities with authority granted to the SEC to further define the term.

In the CFTC's proposed rule "Core Principles and Other Requirements for Swap Execution Facilities," the CFTC requires that a SEF either execute trades on an "order book" or "Request for Quote" system. An order book model is used by exchanges, where numerous bids and offers are aggregated and the market sees the prices at which participants are willing to buy and sell. An RFQ allows a customer to transmit a request for bids or offers to only certain market participants.

The CFTC's rule would require that market participants submit an RFQ to at least 5 other market participants; the SEC's permits an RFQ to go to 1 or more. In addition, the CFTC proposed to prohibit "voice only" transactions—transactions that occur by phone before they are entered into an electronic system. In addition, both the SEC and CFTC require that bids and offers be displayed for a minimum amount of time before execution.

Market participants have expressed concerns that these proposals will reduce liquidity in the swaps markets, by requiring that they make known to the market their trading strategies ahead of execution. This gives others in the market the opportunity to front run the trade, making it more expensive for the counterparty to lay off the risk associated with the transaction. They have argued for more flexibility in mode and method of execution, to allow SEFs to evolve naturally.

The primary provisions in H.R. 2586 prohibit the regulators from requiring a minimum number of participants to receive or respond to quote requests, in line with the SEC's approach. The bill also prohibits the regulators from limiting the means of interstate commerce that market participants can use to execute swaps (i.e. voice only). In addition, H.R. 2586 prohibits the agencies from requiring a SEF to display or delay quotes for any specific period of time.

While SEFs were included in Dodd-Frank as a means to improve the pricing that end-users and other market participants receive on their swap transactions by enhancing transparency, the rigid approach of the CFTC in mandating mode and method of execution will actually have the opposite effect. Contrary to Congress' intent, it could make swaps more expensive for market participants. H.R. 2586 is needed to ensure the regulatory agencies provide enough flexibility, particularly in the initial stages of developing this new market infrastructure, to permit SEFs to evolve naturally toward the best mode of execution, without imposing undue costs on market participants.

#### SECTION-BY-SECTION

Section 1 is the short title, "Swap Execution Facility Clarification Act"

Section 2(a) amends the Commodity Exchange Act to prohibit the Commodity Futures Trading Commission from defining a Swap Execution Facility (SEF) to require a minimum number of participants that receive bids or offers; place a timing requirement on displaying bids or offers; limit the means of interstate commerce used by market participants to enter into or execute swap transactions on the trading system or platform, or require bids or offers on one trading system or platform operated by the SEF to interact with bids and offers on another trading system or platform operated by the SEF.

Section 2(b) has a similar amendment to the Securities and Exchange Act.

Section 3 excludes the amendments made by this bill from the requirements of the Paperwork Reduction Act and from notice and comment requirements of the Administrative Procedure Act.

## COMMITTEE CONSIDERATION

### I. HEARINGS

In the 112th Congress, the Committee has held seven hearings, four Full Committee and two General Farm Commodities and Risk Management Subcommittee hearings to examine the implementation of Title VII of the Dodd-Frank Act and one Full Committee hearing to examine legislative proposals related thereto, including H.R. 2586. The Committee took testimony from witnesses that represented a broad spectrum of participants in the derivatives markets.

In the following hearings, witnesses testified to the importance of clarifying the definition of “swap execution facility” (SEF) to allow SEFs to evolve naturally toward the best mode of execution, without imposing undue costs on market participants:

**Public hearing to review implementation of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act: February 10, 2011**

**Public hearing to review implementation of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Part II: February 15, 2011**

**To review legislative proposals amending Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act: October 12, 2011**

For example, on October 12, Mr. Chris Giancarlo of GFI Group, on behalf of the Wholesale Markets Brokers Association, Americas testified:

“Mr. Chairman, introduction, consideration, and passage of the SEF Clarification Act will provide regulators with a clear expression of Congress’ legislative intent and ensure that the final rules remain within the framework of competitive OTC markets. The WMBAA remains concerned, as it has expressed in its comment letters to the SEC and the CFTC, that limitations on permitted modes of trade execution or requirements to display or delay quotes will cause significant disruptions to OTC swaps markets with the potential to drive trading offshore. We question what substantive analysis has been done on the economic effects of the CFTC proposed rule, which could run up transaction costs in the U.S. swaps markets.”

### II. FULL COMMITTEE

The Committee on Agriculture met, pursuant to notice, with a quorum present, on January 25, 2012, to consider H.R. 2586, to refine the definition of swap execution facility in the provisions regulating swap markets added by title VII of the Dodd-Frank Wall

Street Reform and Consumer Protection Act, and other pending business. Chairman Lucas offered an opening statement, as did Ranking Member Peterson.

By unanimous consent, the Subcommittee on General Farm Commodities and Risk Management was discharged from further consideration and the bill, H.R. 2586 was placed before the Committee for consideration and without objection a first reading of the bill was waived and it was opened for amendment at any point. The Chairman offered an Amendment in the Nature of a Substitute to the bill, and counsel provided a brief explanation of the amendment.

Mr. Peterson was recognized to offer and explain an amendment to expedite implementation by excluding the amendments made by the bill from the requirements of the Paperwork Reduction Act and from notice and comment requirements of the Administrative Procedure Act and modifies the applicable to the CFTC in interpreting or further defining the term "swap execution facility". By a voice vote the Peterson amendment was adopted.

There being no further amendments, the Peterson motion to approve the Amendment in the Nature of a Substitute to H.R. 2586, as amended was adopted by a voice vote.

By a voice vote, the Peterson motion to report the bill favorably to the House with the recommendation that it do pass was adopted.

Chairman Lucas then advised Members that pursuant to the rules of the House of Representatives that Members have 2 calendar days to file such views with the Committee.

Without objection, staff was given permission to make any necessary clerical, technical or conforming changes to reflect the intent of the Committee.

Chairman Lucas thanked all the Members and adjourned the meeting.

#### REPORTING THE BILL—ROLL CALL VOTES

In compliance with clause 3(b) of rule XIII of the Rules of the House of Representatives, H.R. 2586 was reported by voice vote with a majority quorum present. There was no request for a recorded vote.

#### COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee on Agriculture's oversight findings and recommendations are reflected in the body of this report.

#### BUDGET ACT COMPLIANCE (SECTIONS 308, 402, AND 423)

The provisions of clause 3(c)(2) of rule XIII of the Rules of the House of Representatives and section 308(a)(1) of the Congressional Budget Act of 1974 (relating to estimates of new budget authority, new spending authority, new credit authority, or increased or decreased revenues or tax expenditures) are not considered applicable. The estimate and comparison required to be prepared by the Director of the Congressional Budget Office under clause 3(c)(3) of rule XIII of the Rules of the House of Representatives and sections 402 and 423 of the Congressional Budget Act of 1974 submitted to the Committee prior to the filing of this report are as follows:

FEBRUARY 6, 2012.

Hon. FRANK D. LUCAS,  
*Chairman, Committee on Agriculture,*  
*House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 2586, the Swap Execution Facility Clarification Act.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susan Willie.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

*H.R. 2586—Swap Execution Facility Clarification Act*

The Dodd-Frank Wall Street Reform and Consumer Protection Act established entities known as swap execution facilities (SEFs) where multiple parties are able to trade swaps. (A swap is a contract that calls for an exchange of cash between two participants based on an underlying rate or index, or on the performance of an asset.)

H.R. 2586 would amend the definition of an SEF to prevent the regulatory agencies—the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC)—from imposing certain requirements on such facilities. Specifically, the bill would prevent the agencies from developing regulations that require an SEF to follow certain business practices, such as setting a minimum number of participants to receive a bid.

Neither the CFTC nor the SEC has finalized regulations regarding swap execution facilities. Based on information from the two agencies, CBO expects that incorporating the provisions of H.R. 2586 at this point in the regulatory process would not have a significant effect on the workload of either agency. Therefore, CBO estimates that any change in discretionary spending to implement the legislation, which would be subject to the availability of appropriated funds, would not be significant. Further, under current law, the SEC is authorized to collect fees sufficient to offset its appropriation each year; CBO expects that the agency would set fee rates each year to offset amounts provided in appropriation acts. Enacting H.R. 2586 would not affect direct spending or revenues; therefore, pay-as-you-go procedures do not apply.

H.R. 2586 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would impose no costs on state, local, or tribal governments.

On December 14, 2011, CBO transmitted an estimate for H.R. 2586, the Swap Execution Facility Clarification Act, as ordered reported by the House Committee on Financial Services on November 30, 2011. The earlier bill would make similar changes in the definition of a swap execution facility. CBO estimates that enacting either version of the legislation would have an insignificant cost.

The CBO staff contact for this estimate is Susan Willie. The estimate was approved by Theresa Gullo, Deputy Assistant Director for Budget Analysis.

PERFORMANCE GOALS AND OBJECTIVES

With respect to the requirement of clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the performance goals and objectives of this legislation are to refine the definition of swap execution facility in the provisions regulating swap markets added by title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

CONSTITUTIONAL AUTHORITY STATEMENT

The Committee finds the Constitutional authority for this legislation in Article I, section 8, clause 18, that grants Congress the power to make all laws necessary and proper for carrying out the powers vested in Congress by the Constitution of the United States or in any department or officer thereof.

COMMITTEE COST ESTIMATE

Pursuant to clause 3(d)(2) of rule XIII of the Rules of the House of Representatives, the Committee report incorporates the cost estimate prepared by the Director of the Congressional Budget Office pursuant to sections 402 and 423 of the Congressional Budget Act of 1974.

ADVISORY COMMITTEE STATEMENT

No advisory committee within the meaning of section 5(b) of the Federal Advisory Committee Act was created by this legislation.

APPLICABILITY TO THE LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act (Public Law 104–1).

FEDERAL MANDATES STATEMENT

The Committee adopted as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act (Public Law 104–4).

EARMARK STATEMENT REQUIRED BY CLAUSE 9 OF RULE XXI OF THE RULES OF THE HOUSE OF REPRESENTATIVES

H.R. 2586 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9(e), 9(f), or 9(g) of rule XXI of the Rules of the House Representatives.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

**COMMODITY EXCHANGE ACT**

\* \* \* \* \*

**SEC. 1a. DEFINITIONS.**

As used in this Act:

(1) \* \* \*

\* \* \* \* \*

(50) SWAP EXECUTION FACILITY.—**[The term]**

(A) *IN GENERAL.*—*The term “swap execution facility” means 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)]** (i) facilitates the execution of swaps between persons; and

**[(B)]** (ii) is not a designated contract market.

(B) *INTERPRETATION.*—*In interpreting or further defining the term “swap execution facility”, the Commission shall not require a swap execution facility to—*

(i) have a minimum number of participants receive a bid or offer or respond to any method of trading functionality;

(ii) delay bids or offers for any period of time; or

(iii) limit the means of interstate commerce utilized by market participants to enter into and execute any swap transactions on the method of trading functionality.

\* \* \* \* \*

**SECURITIES EXCHANGE ACT OF 1934**

**TITLE I—REGULATION OF SECURITIES EXCHANGES**

\* \* \* \* \*

DEFINITIONS AND APPLICATION OF TITLE

SEC. 3. (a) When used in this title, unless the context otherwise requires—

(1) \* \* \*

\* \* \* \* \*

(77) SECURITY-BASED SWAP EXECUTION FACILITY.—**[The term]**

(A) *IN GENERAL.*—*The term “security-based swap execution facility” means a trading system or platform in which multiple participants have the ability to execute or trade security-based 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)]** (i) facilitates the execution of security-based swaps between persons; and

**[(B)]** (ii) is not a national securities exchange.

*(B) INTERPRETATION.—In interpreting or further defining the term “security-based swap execution facility”, the Commission shall not require a security-based swap execution facility to—*

*(i) have a minimum number of participants receive a bid or offer or respond to any trading system or platform functionality;*

*(ii) display or delay bids or offers for any period of time;*

*(iii) limit the means of interstate commerce utilized by market participants to enter into and execute any security-based swap transactions on the trading system or platform; or*

*(iv) require bids or offers on one trading system or platform operated by the swap execution facility to interact with bids or offers on another trading system or platform operated by the swap execution facility.*

\* \* \* \* \*

## ADDITIONAL VIEWS

For the past year, our Committee has held several hearings and listened to a host of stakeholders who are concerned about how the Dodd-Frank Act is being implemented with regard to improving oversight and accountability in derivative markets. I recommended patience and caution for those seeking to change the law. It is premature to move on legislation until we see the final rules. Looking at the Dodd-Frank rules that have already been finalized by the CFTC, it is safe to say that, so far, the CFTC has done a pretty good job.

The battle over H.R. 2586 is primarily a Wall Street battle. It is between those who currently do most of the swap business—the major banks—and those that wish to challenge them for that business. The CFTC has proposed rules to help open up this market, provide greater pre-trade transparency and lead to greater competition.

Some are concerned that parts of the CFTC's proposed rules governing swap execution facilities (SEFs) are arbitrary or prohibit certain means of swap trading. Others support many aspects of the proposed rule as positive steps toward ensuring these new swaps marketplaces benefit all market participants, not just a few. Attached to these additional views are two letters, one from the Swaps and Derivatives Markets Association and another from the Industrial Energy Consumers of America. *Both organizations oppose H.R. 2586.* All members should review these letters because their concerns merit our attention. These SEFs must be open, transparent marketplaces where competition governs.

To that end, the Peterson Amendment was offered to H.R. 2586. It removed provisions of H.R. 2586 that limit the CFTC's ability to bring transparency to these new markets. *The Peterson amendment does not satisfy the objections of those who oppose H.R. 2586* but it does take a step in the right direction.

Finally, as part of the Peterson Amendment, the Committee approved language that should look very familiar to Farm Bill veterans. It is the exact same provisions that we incorporate in each Farm Bill for implementation of the Title I commodity programs. In that context, it exempts USDA from provisions of the Paperwork Reduction Act and notice and comment provisions of the Administrative Procedures Act.

With this change, comments can still be sent to the CFTC. Anyone would still be able to meet with CFTC officials to share their thoughts on how these bills should be implemented. Farm groups certainly did not have any trouble sharing their views on Farm Bill implementation. Given the openness the CFTC has already demonstrated, this provision will not hurt anyone's ability to provide input to the CFTC.

COLLIN C. PETERSON.  
JOE COURTNEY.  
JAMES P. MCGOVERN.  
CHELLIE PINGREE.  
TIMOTHY J. WALZ.  
JIM COSTA.  
PETER WELCH.



**Industrial Energy Consumers of America**  
*The Voice of the Industrial Energy Consumers*

---

1155 15<sup>th</sup> Street, NW, Suite 500 • Washington, D.C. 20005  
Telephone 202-223-1420 • Fax 202-530-0659 • [www.ieca-us.org](http://www.ieca-us.org)

January 24, 2012

The Honorable Frank Lucas  
Chairman  
Committee on Agriculture

The Honorable Colin Peterson  
Ranking Member  
Committee on Agriculture

**Re: H.R. 2586 – “Swap Execution Facility Clarification Act”**

Dear Chairman Lucas and Ranking Member Peterson:

The Industrial Energy Consumers of America (IECA) is opposed to H.R. 2586, the Swap Execution Facility Clarification Act because it guts transparency and prevents competition – when both are desperately needed. The ‘swap execution facility’ is an important component of Dodd-Frank’s attempt to bring greater transparency to the OTC markets.

We urge Congress to ensure an open and competitive market place for discovering prices. Doing so will benefit end users.

Sincerely,

Paul N. Cicio  
President

cc: Committee on Agriculture

---

*The Industrial Energy Consumers of America is a nonpartisan association of leading Manufacturing companies with \$700 billion in annual sales and with more than 650,000 employees nationwide. It is an organization created to promote the interests of manufacturing companies through research, advocacy, and collaboration for which the availability, use and cost of energy, power or feedstock play a significant role in their ability to compete in domestic and world markets. IECA membership represents a diverse set of industries including: plastics, cement, paper, food processing, brick, chemicals, fertilizer, insulation, steel, glass, industrial gases, pharmaceutical, aluminum and brewing.*



**Industrial Energy Consumers of America**  
*The Voice of the Industrial Energy Consumers*

---

1155 15<sup>th</sup> Street, NW, Suite 500 • Washington, D.C. 20005 202-223-1420

May 24, 2011

David Stawick  
Secretary  
Commodity Futures Trading Commission

Dear Secretary Stawick:

**Re: *Real Time Reporting (RIN number 3038-AD08)***  
***Requirements for Swap Execution Facility (RIN number 3038-AD18)***

On behalf of the Industrial Energy Consumers of America, please accept these comments regarding the CFTC's proposed rules on real time reporting and the requirements for swap execution facilities. Because these proposed rules lie at the heart of the transparency of the OTC derivatives market they are of central concern to the end users that IECA represents.

**About IECA**

The Industrial Energy Consumers of America is a nonpartisan association of leading manufacturing companies with \$800 billion in annual sales and with more than 750,000 employees nationwide. It is an organization created to promote the interests of manufacturing companies through research, advocacy, and collaboration for which the availability, use and cost of energy, power or feedstock play a significant role in their ability to compete in domestic and world markets. IECA membership represents a diverse set of industries including: plastics, cement, paper, food processing, chemicals, fertilizer, insulation, steel, glass, industrial gases, pharmaceutical, aluminum and brewing.

**The Proposed Rules**

IECA's members believe that transparency is critical to ensure that OTC derivatives markets operate to the benefit of the thousands of end users, such as IECA's member companies, that rely on them to hedge risk. At the same time IECA's members appreciate the need to ensure that these markets allow end users to enter into unique, custom tailored risk management contracts for which there may not be a readily liquid tradeable market. It is our belief that the purpose of Dodd Frank was to create the appropriate conditions for both kinds of contracts: bespoke derivatives tailored to the needs of individual companies, and more widely marketable, standardized transactions that might solicit a variety of market interest.

**Real Time Reporting**

IECA members are end users of derivatives. As such it is likely that the reporting requirements of Dodd Frank would in most (though not all) cases fall upon these companies' counterparties, who will most likely be registered as swap dealers. It is worth noting that many IECA companies enter into principal-to-principal trades with other end users, and in such cases would decide among themselves who must report. However in either case, it is apparent that Congress intended the real time reporting rules to serve as a source of transparency in the OTC derivatives markets.

We support the CFTC's proposal that most trades be reported as soon as technologically feasible. We anticipate that for most liquid transactions this will mean trades are reported and publicly available as soon as they are executed. This information will be useful to end users, who will be able to compare prices in different contracts both in order to help their own risk management purposes, as well as gain valuable pricing information for underlying products such as energy or physical commodities.

In the case of block trades, IECA's members understand the concerns of some that certain transactions are so complex as to require execution over an extended period of time. In such circumstances it is alleged that reporting a trade may allow other market participants to "front run" the counterparty (most likely a swap dealer) who is accommodating the trade. It is alleged that this will drive dealers from the market and create illiquidity.

Block trades are not a phenomenon unique to OTC markets. As the Commission knows such trades have been a regular feature of the exchange traded futures markets for many years. Because transparency and liquidity are both important components of a healthy market we urge the CFTC to carefully weigh whether the proposed 15 minute reporting delay for block trades is sufficient to allow market participants to spread out the elements of the most complicated trades. At the same time we expect that the CFTC will rely on its existing expertise and experience with block trades in the futures markets in making any reporting delay for such trades, and we urge the Commission not to be unduly influenced by claims that reporting prices will necessarily lead to non functioning markets.

#### **Requirements for Swap Execution Facilities**

The Dodd-Frank Act requires the CFTC to designate trades that must be cleared when entered into by parties other than end users. When a trade is subject to the clearing requirement Dodd Frank further requires that such trades be executed on a designated contract market, or a swap execution facility, in the case either market makes such a contract available for trading. This latter requirement, the "execution requirement," is an important component of Dodd-Frank's attempt to bring greater transparency to the OTC markets. As such we urge the Commission to be vigilant in ensuring that swap execution facilities provide an open and competitive marketplace for discovering prices. This will benefit end users even considering that end users will not be subject to this requirement.

Dodd Frank defined a "swap execution facility" as "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 facilitates the execution of swaps

between persons; and is not a designated contract market.” By its terms the definition appears to require a SEF to be a central trading market that allows multiple parties to present bids and offers to multiple other parties. It appears that such market is to be open on a nondiscriminatory basis, and transparent to all in illustrating the current market price for traded swaps.

The SEF definition is consistent with the general market architecture of Dodd Frank: the most liquid and widely demanded contracts, which must be cleared, must likewise be traded in an open, transparent and competitive market. Meanwhile transactions which are unique or highly customized, for which there is little demand, can continue to be entered into on a principal-to-principal basis.

End users benefit from this architecture because they have the option of seeking out customized trades, or trading and clearing on a market. Even in the case of transactions an end user does “off facility”, it still benefits because it is able to see the prices at which similar or related trades are executed. The SEF requirements thus have an important role both for registered market participants like swap dealers and major swap participants, as well as end users.

Because SEFs are a cornerstone of the new, open and transparent OTC markets created by Dodd Frank we urge the Commission to require SEFs to allow multiple parties to see and make quotes to other multiple parties in an open and publicly available forum. Request for quote systems, which allow a dealer to solicit prices in a closed, non-transparent proprietary market, do not appear to meet either the literal terms of the SEF definition or the larger goals of Dodd Frank. We urge the Commission to require that SEFs operate in a manner that publicly reveals market prices. Doing otherwise, such as preserving the “one-to-one” pricing model of existing dealer systems, would merely ratify the status quo and appear to be inconsistent with the goal of Wall Street reform.

#### **Conclusion**

Transparency and the ability to enter into unique transactions are both vitally important to derivative end users. We believe Dodd Frank’s primary goal with respect to derivatives reform was to provide both. Thus we respectfully request that in the areas related to transparency, such as the real time reporting and swap execution facility requirements, the Commission seek to create open, transparent markets that provide vital information to end users. At the same time the Commission should ensure that end users can access unique risk management products tailored to their individual needs.

Thank you for considering our comments, and please know we are available to provide any further information.

Sincerely,

Paul Cicio  
President



November 29, 2011

Hon. Spencer Bachus  
Chairman

Hon. Barney Frank  
Ranking Member

United States Congress  
House Committee on Financial Services  
2129 Rayburn House Building  
Washington, DC 20515

Re: In Opposition to H.R. 2586 the "Swap Execution Facility Clarification Act"

Dear Chairman Bachus and Ranking Member Frank:

The Swaps & Derivatives Market Association ("SDMA") strongly opposes H.R. 2586 the "Swap Execution Facility Clarification Act."

We oppose this Bill because it will continue "business as usual" in the swaps market, stifling competition among dealers, dangerously limiting fair dealing, keeping transaction prices artificially high, and importantly, impeding liquidity and increasing systemic risk. The CFTC must be allowed to complete their task to implement Title VII of the Dodd-Frank Act to ensure that the swaps markets open up and no longer represent a threat to the US economy.

The SDMA is a non-profit financial trade group comprised of many US and internationally based Broker-Dealers, Investment banks, Futures Commission Merchants and Asset Managers participating in all segments of the exchange-traded and over-the-counter derivatives and securities markets. The SDMA supports the goals of Title VII of the Dodd-Frank Act.

To be clear, H.R. 2586 will override critical pre-trade price transparency requirements that require that swap dealers and market participants display their prices to the marketplace before a trade occurs. HR 2586 provides that SEFs are not required to (1) disclose a bid or offer to a minimum number of participants, and (b) "display or delay bids or offers for any period of time".

To remove such a requirement will have several negative consequences.

**Fair Dealing**

To ensure that market participants have equal access to best pricing, simply put, they must know what the price is before buying or selling. To shield, conceal or distribute such a price selectively, as would be permitted under HR 2586, destroys trust and integrity in the capital markets. It would also prevent market participants from determining the *fair value* of a transaction before entering in the trade.

Lack of pre-trade price transparency increases systemic risk.

As empirical experience and academic research show, the dissemination of live, actionable prices to all market participants simultaneously increases market integrity, promotes a level playing field, and increases liquidity.

**Fostering Competition & Lowering Transaction Costs**

It is well established in any market place-be it swaps, bonds, equities or cell phones-that competition among merchant providers forces transaction costs lower and drives liquidity higher. By now requiring incumbent dealers to compete with each other and other new price providers directly drives transaction costs lower and fosters optimal execution.

By contrast, HR 2586 would increase transaction costs.

By fostering greater pre and post trade transparency, it is estimated that such transaction costs will fall by 30% or at least \$15 Billion annually in the first few years after Dodd Frank.

That is \$15 Billion that corporations can use on their own balance sheets to invest in research and development or hire more workers.

That is \$15 Billion that loan portfolios can pass back to consumers in the form of cheaper small business loans or cheaper mortgages for American families.

**Higher Liquidity means Lower Risk to the US Economy**

To ensure increased liquidity, Congress should seek to promote greater competition and transparency as well as a more level playing field. Fair and open markets attract more dealers and buy-side participants which, in turn, foster even greater liquidity. As evidenced by Financial Crisis of 2008, the credit default and interest rate swap markets can never have enough liquidity.

**Current Rules Do Promote SEF Flexibility**

The SEC and CFTC have mindfully permitted different execution methods such as exchange-like anonymous Central Limit Order Books and Request for Quote methodologies. Contrary to what you have been told, the Commissions do not restrict voice/hybrid broking methodologies. They merely require that they operate with certain pre-trade transparency precepts in mind.

S. Bachus  
B. Frank  
November 29, 2011  
Page 3

The Commissions have wisely allowed the markets the flexibility to decide which method works best in each market context.

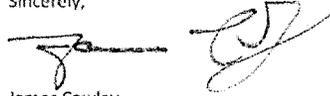
The SDMA, too, has several voice broker constituent firms with many hundreds of voice brokers. After our review, we support the Dodd Frank Act as passed.

Conclusion

To be clear, the current SEF rules promote transparency, fair dealing and lower transaction costs.

You must vote against H.R. 2586 and grant the CFTC the opportunity to make these markets safer for the American public.

Sincerely,



James Cawley  
The Swaps & Derivatives Market Association  
(646) 588-2003

○