



Request for No-Action Relief from Trade Execution Requirement

October 15, 2014

Mr. Vincent A. McGonagle
Division of Market Oversight
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, DC 20581

Re: Request for Relief from the Trade Execution Requirement for Categories of Package Transactions under CFTC Staff No-Action Letter 14-62

Dear Mr. McGonagle,

Managed Funds Association (“**MFA**”)¹ respectfully requests the no-action relief described below with respect to the three categories of package transactions described and defined in the Commodity Futures Trading Commission (the “**Commission**” or “**CFTC**”) No-Action Letter 14-62² issued by the Division of Market Oversight (“**DMO**”) and Division of Clearing and Risk (the “**Divisions**”) for which relief expires on November 15, 2014.³ While MFA appreciates the

¹ Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent and fair capital markets. MFA, based in Washington, DC, is an advocacy, education and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, the Americas, Australia and many other regions where MFA members are market participants.

² See CFTC Staff No-Action Letter No. 14-62, “No-Action Relief from the Commodity Exchange Act Sections 2(h)(8) and 5(d)(9) and from Commission Regulation § 37.9 for Swaps Executed as Part of Certain Package Transactions and No-Action Relief for Swap Execution Facilities from Compliance with Certain Requirements of Commission Regulations § 37.9(a)(2), § 37.203(a) and § 38.152 for Package Transactions”, issued May 1, 2014 (“**NAL 14-62**”).

³ These three categories include: (1) package transactions in which the components include at least one individual swap component that has been “made available to trade” (“**MAT**”) and is subject to the trade execution requirement; and at least one individual swap component that is under the Commission’s exclusive jurisdiction and not subject to the Commission’s clearing requirement (“**MAT/Non-MAT Uncleared Package Transactions**”); (2) package transactions in which the components include at least one individual swap component that has been MAT and is subject to the trade execution requirement; and at least one individual component that is not a swap (other than U.S. Dollar Swap Spreads, as defined in NAL 14-62) (“**MAT/Non-Swap Instruments Package Transactions**”); and (3) package transactions which include at least one individual swap component that has been MAT and is subject to the trade execution requirement; and at least one individual swap component that is a swap over which the Commission does not have exclusive jurisdiction (“**MAT/Non-CFTC Swap Package Transactions**”). Collectively, we refer to these categories as the “**November 15 Package Transactions**”.

Divisions' grant of no-action relief under NAL 14-62 to phase in the trade execution requirement for different types of package transactions, we believe that DMO should permit an alternative execution paradigm for the November 15 Package Transactions and that the compliance timeline should be extended further for the November 15 Package Transactions until February 15, 2015.

MFA remains strongly committed to the goals of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act.⁴ Nonetheless, as we have outlined in prior submissions to the Commission,⁵ there are a number of barriers to trading of certain package transactions on registered swap execution facilities (“SEFs”) and designated contract markets (“DCMs”)⁶ related to infrastructure, regulation, and market participant preparedness. While the industry has made progress - SEFs now list certain package transactions and market participants now trade certain package transactions on SEFs - many challenges remain with respect to the November 15 Package Transactions. Unfortunately, these issues will not, we believe, be resolved by November 15. We therefore request that DMO issue the no-action relief described below.

I. Request for Relief

As has been described in a number of comment letters from market participants and industry associations⁷, the impediments presented when a component leg in a package transaction is a MAT swap vary with the type of package transaction in question. The Commission has generally recognized two types of impediments with respect to package transactions: challenges with the *processing* of such transactions by futures commission merchants (“FCMs”) and derivatives clearing organizations (“DCOs”) and challenges in *facilitating trade execution* by SEFs and DCMs.⁸

⁴ Pub. L. 111-203, 124 Stat. 1376 (2010).

⁵ See Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Chairman Massad, CFTC, July 30, 2014, available at: <https://www.managedfunds.org/wp-content/uploads/2014/07/MFA-Welcome-Letter-to-CFTC-Chair-Massad-Final.7.30.14.pdf>; Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Vincent A. McGonagle, Division of Market Oversight, CFTC, April 23, 2014, available at: <https://www.managedfunds.org/wp-content/uploads/2014/04/ICE-Submission-on-Packaged-Transactions-MFA-Final-Letter.pdf>; and Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Vincent A. McGonagle, Division of Market Oversight, CFTC, January 24, 2014, available at: <https://www.managedfunds.org/wp-content/uploads/2014/01/Packaged-Transactions-NAL-Final-MFA-Letter.pdf>.

⁶ All references to SEFs in this letter shall also refer to DCMs.

⁷ We refer the Divisions to the series of comment letters from market participants and industry associations located at, for example, <http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1409>, which, in relevant part, discuss in detail the nature, utility, benefits and *bona fide* business purposes for package transactions. With respect to the submitted comment letters, we refer the Divisions, in particular, to the letter to the Commission from MFA, dated November 21, 2013, regarding Industry Filings IF 13-004, 13-005, and 13-007 (the “MFA MAT Letter”) and the letter to the Commission from Citadel LLC, dated November 29, 2013 (the “Citadel Letter”). While we do not restate in this letter all of the points made in the MFA MAT Letter and the Citadel Letter, we respectfully request that DMO views the relief request in this letter in light of the comments in both letters concerning package transactions.

⁸ See NAL 14-62 at p. 3.

The industry has made substantial progress in advancing solutions that address the challenges with the *processing* of such transactions by FCMs and DCOs.⁹ However, these solutions have not yet been fully implemented by all relevant parties, as the Commission acknowledged in CFTC No-Action Letter No. 14-121, issued on September 30, 2014.¹⁰ In addition, these *processing* challenges were largely related to multi-swap package transactions for which relief expired on May 16, 2014¹¹ and June 2, 2014.¹²

Based on the SEF trading experience of our members to date, the challenges in *facilitating trade execution* remain in many cases, and acutely so with respect to November 15 Package Transactions. These challenges vary depending on the type of package transactions in question. In Section II below, we set forth examples of package transactions within the three categories of November 15 Package Transactions and explain the associated challenges with respect to their SEF execution.

To enable their continued execution, we request no-action relief from DMO that would permit each MAT swap component of a November 15 Package Transaction to be executed off-SEF, but subject to the rules of a SEF. This alternative execution paradigm would allow market participants to continue to quote and execute such package transactions *as a package*. In conjunction with this request, we further seek time-limited no-action relief from the trade execution requirement for November 15 Package Transactions until February 15, 2015, to allow market participants a reasonable period of time to implement the proposed new execution paradigm. We outline the details of our request below.

In the absence of the relief requested in this letter, we are very concerned that November 15 Package Transactions will become largely unavailable as an investment or risk management tool to a significant number of market participants upon the expiration of the remaining relief in NAL 14-62. Our concerns would be materially amplified if and when the scope of MAT swaps is expanded.

⁹ We refer, for example, to the inclusion of package transaction enhancements in FpML version 5.7 which was released on July 9, 2014. See <http://www2.isda.org/news/isda-publishes-recommendation-for-fpml-version-57>.

¹⁰ See CFTC Staff No-Action Letter No. 14-121, "Extension of No-Action Relief for Swap Execution Facilities and Designated Contract Markets from Compliance with Certain Requirements of Commission Regulations § 37.9(a)(2), § 37.203(a) and § 38.152 for Package Transactions", issued on September 30, 2014, available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/14-121.pdf>.

¹¹ Relief expired on May 16, 2014 for package transactions in which each component has been MAT and is subject to the trade execution requirement. See NAL 14-62 at p. 4, fn. 16.

¹² Relief expired on June 2, 2014 for package transactions in which the components include at least one MAT swap component that is subject to the trade execution requirement and each of the other swap components is subject to the CFTC's clearing requirement. See NAL 14-62 at p. 4.

II. Scope of Products Subject to Requested Relief

(a) MAT/Non-MAT Uncleared Package Transactions

A common package transaction in this category that is not generally supported on any SEF is a **swap versus swaption** package transaction.

- No SEFs “list”¹³ swap vs. swaption package transactions on an order book or electronic request-for-quote (“**RFQ**”) platform.
- The swaption component of the transaction is uncleared. Buy-side market participants do not generally trade uncleared interest rate swaps on SEFs. Further, as an uncleared swap, it is thus potentially subject to the CFTC’s swap trading relationship documentation requirements.¹⁴ Typically, the swaption component trades under an International Swaps and Derivatives Association, Inc. (“**ISDA**”) Master Agreement. At present, SEF rules can be interpreted to require parties desiring to trade these package transactions to have swap trading relationship documentation in place, such as ISDA Master Agreements. However, this documentation requirement could be deemed an “enablement mechanism” for the MAT swap component that is intended to be cleared, which would appear to violate SEF impartial access requirements.¹⁵ Second, because the swaption component trades under an ISDA Master Agreement, market participants can only trade a swap vs. swaption package transaction on a name-disclosed basis, which gives rise to further concerns about impartial access.¹⁶ Third, under Commission regulations and related staff interpretations, we understand that if an uncleared swap is executed on or pursuant to the rules of a SEF, the SEF must provide a confirmation that contains all of the terms of the swap transaction.¹⁷ To satisfy this requirement after the expiration of the current no-action relief on September 30, 2015,¹⁸ a SEF may incorporate by reference all of the terms of the relevant ISDA Master Agreement in the confirmation,

¹³ We use the term “list” in this letter to refer to the actual listing of the relevant package transaction on a SEF, as distinguished from a SEF’s claim to facilitate its execution, or by a SEF’s listing the individual legs of the package transaction rather than the package as a whole.

¹⁴ See CFTC Regulation § 23.504.

¹⁵ See CFTC 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, November 14, 2013, at p. 2 (“SEFs that apply or support enablement mechanisms that allow certain participants to interact with only certain other participants, or to interact in only certain ways, while other participants have broader abilities to interact, are imposing or allowing different access terms on similarly situated participants and are therefore engaging in prohibited discriminatory treatment.”).

¹⁶ *Id.*

¹⁷ See 17 C.F.R. § 37.6(b).

¹⁸ See CFTC Staff No-Action Letter No. 14-108, “Staff No-Action Position Regarding SEF Confirmations and Recordkeeping Requirements under Certain Provisions Included in Regulations 37.6(b) and 45.2”, issued on August 18, 2014, available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/14-108.pdf>.

provided that the ISDA Master Agreement is submitted to the SEF ahead of execution.¹⁹ As a result, buy-side participants would be required to disclose the terms of all of their ISDA Master Agreements to SEFs, which raises material concerns regarding confidentiality and practicality.

- We understand that certain SEFs facilitate trading of swaps vs. swaptions, but execution occurs only through voice RFQ protocols. As the Commission is aware, the SEFs that offer such execution protocols transact dealer-to-dealer business, almost exclusively. Such SEFs still have few, if any, buy-side participants. Consequently, such facilitation is of limited utility, as it does not offer a solution to the market as a whole.

(b) MAT/Non-Swap Instruments Package Transactions

Common package transactions in this category that are not supported on any SEF include:

- **Mortgage-Backed Security (“MBS”) basis package transactions**, which involve Agency MBS vs. swaps.
 - No SEFs currently “list” MBS basis package transactions on an order book or an electronic RFQ platform.
 - We are aware of one SEF with an affiliate that operates an electronic trading platform for MBS and has plans to leverage that platform to offer SEF trading of MBS basis package transactions. Unfortunately, we believe that this solution will not be fully developed or robustly implemented by November 15.
- **Swaps vs. futures package transactions**²⁰ generally, including both **invoice spreads**, which consist of T-note or T-bond futures vs. swaps (including Market Agreed Coupon, or MAC, swaps), and **cash/futures basis packages**, which consist of Eurodollar futures bundles vs. swaps. With respect to invoice spreads:
 - No SEFs currently “list” invoice spreads.
 - Since futures contracts can only be listed on a DCM, a non-DCM is legally prohibited by Commission regulation from listing an invoice spread.
 - We understand that one DCM plans to list swaps alongside its futures contracts, and then offer inter-commodity spread contracts between the two. Unfortunately, we expect that this solution will not be fully developed or robustly implemented by

¹⁹ See Commission Final Rule, “Core Principles and Other Requirements for Swap Execution Facilities”, 78 Fed. Reg. 33491(June 4, 2013), at 33491, fn. 195.

²⁰ We are separately concerned that new CME Rule 538 does not permit a MAT swap to be the related position for an Exchange for Related Position (“**EFRP**”) transaction.

November 15. Presuming that this DCM's solution is eventually developed and implemented, a central limit order book ("**CLOB**") would be the only permitted mode of execution for such invoice spreads executed on the DCM, to the exclusion of RFQ execution. Further, we are aware of only one DCM that intends to try to offer this solution, which could raise competitive concerns.

- **Non-USD swap spreads**²¹, including spreads with Euro-denominated sovereign debt.

(c) **MAT/Non-CFTC Swap Package Transactions**

A common package transaction product in this category is an **index CDS vs. single-name CDS**.

- No SEFs currently "list" index CDS vs. single-name CDS package transactions.
- The single-name CDS component of the transaction is an uncleared security-based swap that trades under an ISDA Master Agreement. We believe that the same three resulting challenges to SEF execution (*i.e.*, enablement mechanisms, name-disclosed basis and confirmation confidentiality and practicality concerns), as discussed above with respect to swaps vs. swaption packages, are also presented for index CDS vs. single-name CDS packages.
- Because the single-name CDS component is subject to the jurisdiction of the Securities and Exchange Commission ("**SEC**"), it is uncertain how and when the SEC's final regulatory regime for security-based SEFs will emerge, and how dually registered SEFs will be regulated.

III. Mechanics of Requested Relief

We believe that the most comprehensive way to preserve liquidity in all three categories of November 15 Package Transactions is for the CFTC to permit the MAT swap component of these package transactions to be executed off-SEF, but subject to the rules of a SEF. Similar models have worked well in the futures and equities markets.²²

The terms of November 15 Package Transactions could be negotiated between market participants away from the SEF. But the execution of the MAT swap leg would be subject to the rules of the SEF. This means that the execution of the MAT swap leg would not occur until it had been submitted to the SEF and passed the relevant pre-execution credit checks, among other requirements. The MAT swap leg of the package transaction would then follow the required straight-through processing in the execution-to-clearing workflow. The non-

²¹ A "swap spread" is a package of U.S. or non-U.S. government securities vs. swaps typically with similar tenors.

²² Examples include the EFRP model in the futures market and the qualified contingent trade model in the equities market.

MAT swap legs of the package transactions would be settled away from the SEF based on existing arrangements between the executing counterparties.

We believe such a regime can achieve an appropriate balance between regulatory oversight and orderly, liquid markets. It is difficult to see how any other approach to the infrastructure and regulatory challenges at hand can be overcome without lengthy disruption in the market for these products. We also believe that it would take the markets some reasonable period of time to adjust to this new execution paradigm. Accordingly, we request an extension of the relief in NAL 14-62 for November 15 Package Transactions until February 15, 2015.

IV. Proposed Conditions for Relief

We believe it would be reasonable and appropriate for DMO to determine that, in order to rely on the relief requested in this letter, a market participant executing a November 15 Package Transaction must:

- (a) in addition to satisfying the obligations to which it is subject under Commission Regulation 45.2, record completely and systematically the execution of all MAT swaps that are entered into by it as components of package transactions executed in reliance upon the relief requested in this letter;
- (b) keep all such records in electronic form, or in paper form if originally created and exclusively maintained in paper form, so long as they are retrievable as described herein;
- (c) keep all such records readily accessible via real-time electronic access throughout the life of the swap and for two years following the final termination of the swap; and
- (d) ensure that all such records are retrievable by such market participant in accordance with the requirements of Commission Regulation 45.2(e).

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For the reasons given above, MFA requests that DMO issue the no-action relief described herein.

Certification Pursuant to Commission Regulation 140.99(c)(3)

As required by Commission Regulation 140.99(c)(3), we hereby (i) certify that the material facts set forth in this letter are true and complete to the best of our knowledge; and (ii) undertake to advise the Commission, prior to the issuance of a response hereto, if any material representation contained herein ceases to be true and complete.

We appreciate DMO staff's consideration of the requests set forth in this letter. Please feel free to call Laura S. Harper, MFA's Assistant General Counsel, or the undersigned at (202) 730-2600 with any questions regarding this letter.

Respectfully,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President, Managing Director &
General Counsel

cc:

The Hon. Timothy G. Massad, Chairman
The Hon. Mark P. Wetjen, Commissioner
The Hon. Sharon Y. Bowen, Commissioner
The Hon. J. Christopher Giancarlo, Commissioner