

February 13, 2012

Mr. David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW  
Washington, DC 20581

Re: Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available to Trade – RIN 3038-AD18

Dear Mr. Stawick:

Markit<sup>1</sup> is pleased to submit the following comments to the Commodity Futures Trading Commission (the “**CFTC**” or “**Commission**”) on the proposed rulemaking to implement certain requirements included in Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “**DFA**”)<sup>2</sup> titled Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available To Trade (the “**Proposed Rule**”).<sup>3</sup>

## Introduction

Markit is a service provider to the global derivatives markets, offering independent data, valuations, risk analytics, and related services for swaps and security-based swaps across many regions and asset classes in order to reduce risk, increase transparency, and improve operational efficiency in these markets. We support the objectives of the DFA, and the Commission’s objectives of increasing transparency and efficiency in the OTC derivatives markets, of reducing both systemic and counterparty risk, and of detecting any market manipulation or abuse.

## Executive Summary

Under the Proposed Rule, if a swap is subject to mandatory clearing and a swap execution facility (“**SEF**”) or designated contract market (“**DCM**”) determined that such swap is “made available to trade” (a “**MAT Determination**”), that swap must be executed on a SEF or DCM, unless another exemption applies. We believe that these MAT Determinations will be a very critical component of the DFA regime and therefore appreciate that the Commission issued further guidance on the process for making such determinations.

However, we have several concerns with the process set forth in the Proposed Rule. Specifically, we believe that: (1) MAT Determinations should be contingent upon, but independent from, mandatory clearing determinations (as proposed) because they will have different effects on the market and will require different types of analysis; (2) MAT Determinations should be based on all enumerated factors, instead of any one, and the Commission should establish objective, measurable standards for applying the facts to those factors; (3) mandatory SEF or DCM execution should be phased-in by identifying an initial set of the

---

<sup>1</sup> Markit is a financial information services company with over 2,400 employees in North America, Europe and Asia Pacific. The company provides independent data and valuations for financial products across all asset classes in order to reduce risk and improve operational efficiency. Please see [www.markit.com](http://www.markit.com) for additional information.

<sup>2</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).

<sup>3</sup> Process for a Designated Contract Market or Swap Execution Facility to Make a Swap Available To Trade, 76 Fed. Reg. 77728 (Dec. 14, 2011).

most liquid swaps that should be considered MAT and holding any other MAT Determinations for 12 months while the market adjusts to the impact of mandatory on-facility trading; (4) MAT Determinations should be subject to review by the Commission on a quarterly basis, and illiquid swaps should be de-classified as MAT; (5) MAT Determinations should always be subject to public notice and comment; and (6) the Commission, rather than SEFs or DCMs, should make the ultimate MAT Determinations, not only because it will have market-wide data, but also because individual SEFs and DCMs may have an economic interest in making a MAT Determination for each and every swap, regardless of its liquidity.

## Comments

### 1. MAT Determinations Should Be Independent from Mandatory Clearing Determinations and Should be Granular

Several panelists at the January 30, 2012 roundtable discussed whether or not swaps should be automatically considered MAT if they are subject to mandatory clearing. According to some panelists, the factors relevant to an MAT Determination are similar to those to be considered for a mandatory clearing determination.<sup>4</sup> As an initial matter, we believe that the factors for these determinations differ in several material respects. Specifically, while the MAT factors all tend to relate to the liquidity of a given swap, liquidity is only one of several factors in the mandatory clearing factors.

In any event, we believe that the MAT Determinations and mandatory clearing determinations should be distinct from one another because they will have different effects on the market and will necessarily require different types of considerations. Swaps with even a limited amount of liquidity could potentially become subject to mandatory clearing without disrupting the market, but a mandate to trade certain less liquid swaps through a SEF requiring pre-trade transparency could effectively kill liquidity in those instruments and disrupt market functioning. While we agree with several of the panelists who argued that most swaps subject to mandatory clearing will most likely be *listed* by SEFs or DCMs, we do not believe that they should automatically be subject to *mandatory on-facility trading* because of these effects.

We also believe that separating mandatory clearing determinations and MAT Determinations is consistent with the DFA. Section 2(h)(8) of the Commodity Exchange Act, as modified by the DFA, requires all swaps subject to mandatory clearing to be executed on a SEF or DCM *unless no SEF or DCM makes the swap available to trade*.<sup>5</sup> Congress could not have intended for swaps subject to mandatory clearing to be automatically considered to be MAT if it excluded from the trading requirement those swaps which are subject to mandatory clearing *but which are not MAT*.<sup>6</sup> Moreover, sections 2(h)(1) and 2(h)(2), which deal with mandatory clearing determinations, do not mention the MAT Determination at all.

We also believe that these determinations should be distinct from one another because they will require differing levels of granularity. While differing tenors of a given swap will likely be able to be cleared if any tenor of that swap is cleared, differing tenors of a given swap will have significantly different levels of liquidity. As a result, we believe that MAT Determinations should be performed at levels that are sufficiently granular in order to reflect differences in liquidity between variations of a given swap. In order

---

<sup>4</sup> These factors are provided for in section 2(h)(2)(D) of the CEA and in the Commission's final rule on the subject. See Process for Review of Swaps for Mandatory Clearing, 76 Fed. Reg. 44464 (July 26, 2011).

<sup>5</sup> Commodity Exchange Act, 7 U.S.C. § 2(h)(8).

<sup>6</sup> This is further evidenced by a colloquy where Senator Blanche Lincoln, discussing the interpretation of the phrase "makes the swap available to trade," stated that "[t]he CFTC could consider, for example, whether there is a minimum amount of liquidity such that the swap can actually be traded on the facility. The mere 'listing' of the swap by a swap execution facility, in and of itself, without a minimum amount of liquidity to make trading possible, should not be sufficient to trigger the Trade Execution Requirement." Congressional Record, 111th Congress (2009-2010), July 15, 2010, p. S5923.

to reduce the time and effort required to submit and approve MAT Determinations, however, and as we have previously argued,<sup>7</sup> we believe that MAT Determinations should be made for individual swaps and applied to “buckets” of maturities and tenors (*i.e.* groups of maturities and tenors for a given swap that have similar liquidity measures).

## **2. MAT Determinations Should be Based on Objectively Measurable Factors**

Because we believe that MAT Determinations should be closely tied to the liquidity of a given swap, we appreciate that the list of factors to consider in making an MAT Determination largely relate to a swap’s liquidity.<sup>8</sup> However, we note that the Proposed Rule only requires SEFs and DCMs to “consider” the factors “as appropriate,” and lists the factors in the disjunctive.<sup>9</sup>

We do not believe that this provides sufficiently meaningful guidance. Especially when considering the Commission’s limited ability to deny MAT Determinations, as discussed below, this standard would effectively give SEFs and DCMs unfettered discretion in making MAT Determinations for swaps almost regardless of their actual liquidity. Instead, if SEFs and DCMs are tasked with making MAT Determinations, we believe that the Commission should require them to consider *each* listed factor and should create objective standards such that a swap will become MAT when it breaches a certain liquidity threshold.

While establishing objective liquidity measurements can be challenging, as a provider of Liquidity Scores for a variety of financial products, we have considerable experience in making these types of liquidity determinations. Our experience has shown that, although creating liquidity measures for products that trade mainly over-the-counter is complicated, they can be derived from a combination of observable factors including, but not limited to, trade frequency, average transaction size, bid/offer spread and the number of market makers. We would of course be willing to discuss these matters further with the Commission.

## **3. MAT Determinations and Mandatory SEF or DCM Execution Should be Phased-In Based on Data Analysis**

MAT Determinations will not only impact the liquidity of the swaps market but will also result in other, currently unknown, changes to market structure. Thus, we believe that MAT Determinations, and the associated trading mandate, should initially apply to only a small number of the most liquid swaps that can trade electronically without potentially disrupting the market. Once that initial set of MAT swaps is determined, we believe that the impact of such designation should be observed for a period of 6 to 12 months before any additional swaps are determined to be MAT. This is because every change to the universe of mandatory traded swaps will require significant adjustments from market participants and trading venues.

This way, the Commission and market participants could observe the market impact of MAT Determinations before going forward with other sets of instruments or modifying the Commission’s rule set. The industry would also have an opportunity to judge whether swaps that were believed to be economically equivalent trade with similar liquidity and at the same price.

---

<sup>7</sup> See Letter from Markit to the Commission, 2 (March 8, 2011) (“Liquidity for shorter maturities, however, might be sparse, and liquidity for longer maturities will only exist up to a certain maturity. Declaring all maturities “available for trading” would compromise efforts to develop a market for less liquid maturities within a product that is already determined to be “available for trading” based on more liquid maturities. We urge the Commission to limit any decisions that swaps are “available for trading” to specified maturity buckets or to use certain maturity cut-off points.”).

<sup>8</sup> See Proposed Rule, 76 Fed. Reg. at 77737 (to be codified at 17 C.F.R. § 37.10(b)).

<sup>9</sup> See *id.* (“ . . . a swap execution facility shall consider, as appropriate, the following factors with respect to such swap. . . .”).

We note that this approach would be in keeping with the implementation of Finra's Trade Reporting and Compliance Engine ("**TRACE**"), which relates to the bond market. The rollout of TRACE was accomplished through a methodical process that provided ample time for regulators to measure the impact on liquidity of each step before entering the next phase. TRACE's limited pilot was carefully enlarged over several years through a series of increments, each of which included a larger section of the bond market. Moreover, a control group of bonds was created to be able to compare the liquidity of those bonds where post-trade prices were publically disseminated to some others whose trade prices were not released. We believe that creating such a control group for swaps that are determined to be MAT would greatly aid in observing and mitigating any negative impact of MAT Determinations.

#### **4. MAT Determinations Should be Subject to Regular Reviews By the Commission**

The liquidity of a given swap, or even the entire swaps market in certain circumstances, can vary widely over time. As a result, a swap that trades actively today might quickly become illiquid in the future, and *vice versa*.<sup>10</sup> Because we believe that MAT Determinations should be reserved for the most liquid swaps, we also believe that there must be an efficient method to remove an MAT classification from a given swap when its liquidity drops.

We believe this should be achieved through quarterly reviews of each MAT swap. Specifically, we believe these reviews should analyze a series of objective criteria including, but not limited to, whether: (i) the number of market makers has diminished; (ii) bid/offer spreads have widened significantly; (iii) the frequency with which the swaps are entered into has been reduced; (iv) the average size of the swaps has changed; and (v) the number of execution venues with an active two-sided market in the instrument has changed.

Regardless of the frequency with which these reviews are made or the process utilized for making them, we believe that the Commission, rather than SEFs or DCMs, must make these periodic assessments. Not only will the Commission have market-wide data on activity in the relevant swaps, but it would likely create a significant amount of market confusion if one SEF determines that a given swap should not be MAT while another SEF determines it should be MAT based on their respective views on liquidity of this swap.

#### **5. MAT Determinations Should be Subject to Public Notice and Comment**

We believe that MAT Determinations should be subject to public notice and comment, just as mandatory clearing determinations will be.<sup>11</sup> This notice and opportunity for comment will be especially important if SEFs and DCMs were to make MAT Determinations because public comment will limit the possibility that SEFs and DCMs made such determinations simply to increase their revenue.

#### **6. The Commission Should Ultimately Determine Which Swaps are Made Available To Trade**

We share the concerns voiced by many commenters<sup>12</sup> and panelists at the Commission's roundtable on January 30, 2012 regarding the proposed approach whereby SEFs and DCMs, rather than the

---

<sup>10</sup> Examples include a benchmark 10 year interest rate swap after it turned into a 9 year and 11 month swap in a month from now, or an on-the-run CDX credit index that will becomes an off-the-run credit index in 2 months from today.

<sup>11</sup> See 7 U.S.C. § 2(h)(2).

<sup>12</sup> The Proposed Rule lists nine commenters who requested that the Commission, rather than SEFs or DCMs, determine whether a particular swap is available to trade and three commenters who requested that SEFs and/or DCMs make this determination. See Proposed Rule, 76 Fed. Reg. at 77730 fn. 21-22. Despite the support for a Commission-originated MAT Determination, the Proposed Rule would impose this requirement on SEFs and DCMs. See Proposed Rule, 76 Fed. Reg. at 77737 (to be codified at

Commission, would play the leading role in determining which swaps should be subject to mandatory on-facility execution. This is particularly troublesome considering the Commission's limited ability to deny MAT Determinations under the Proposed Rule.<sup>13</sup> First, individual SEFs and DCMs will not have access to market-wide data on any given swap and therefore may not have an accurate understanding of its liquidity. Indeed, we believe that data from over-the-counter swaps may be an important component to consider when making an MAT Determinations, and individual SEFs and DCMs will not likely have access to this data. Second, it is unclear why SEFs and DCMs, who have the greatest economic incentive in moving all swaps onto facilities, should have the power to determine which swaps should be legally required to be traded on a SEF or DCM.

Therefore, as we stated in a previous comment letter,<sup>14</sup> we believe that the Commission should make the ultimate decision as to which swaps are MAT (based on submissions made by SEFs and DCMs), in a manner similar to the process used for mandatory clearing determinations. Specifically, we believe that the following process should be employed: (1) the swaps that are currently traded on SEFs should be deemed submitted to the Commission for designation approval; (2) the Commission may make its own determination; and (3) once 6 to 12 months have passed, SEFs and DCMs should be permitted to submit their belief as to which swaps should receive an MAT Designation. If such submission is made: (a) the Commission should review such the submission, taking into account each MAT factor; and (b) provide at least a 30-day public comment period regarding its determination as to whether the swap should be determined to be MAT.

We believe that having the Commission make the ultimate MAT Determinations would provide several benefits:

- First, this approach would ensure that MAT Determinations are made consistently, giving relatively equal weight to the various factors described in Proposed Rules 37.10(b) and 38.12(b).<sup>15</sup> On the contrary, if the various SEFs and DCMs each individually make their own MAT Determinations without meaningful oversight by the Commission, each SEF or DCM would likely give different weight to a single factor for the same exact product.
- Second, we believe that this process would give the Commission more time to consider which swaps should be subject to mandatory on-facility trading based on their liquidity. As proposed, SEFs and DCMs can self-certify an MAT Determination under Rule 40.6, giving the Commission only 10 business days to review such determination.<sup>16</sup> These submissions could prove to be extremely lengthy and complex, particularly if SEFs or DCMs are required to provide a separate analysis of the enumerated factors for each swap with a different effective date and/or tenor, as appears to be the case under the Proposed Rule.<sup>17</sup> Therefore, we do not believe that 10 business

---

17 C.F.R. §§ 37.10(a), 38.12(a)). The Commission states that it considers this to be a "balanced approach" but does so without providing any analysis as to the impact of both options except to say that the proposed approach would have the "facilities that may be most familiar with the trading of these swaps" to make the determination. See Proposed Rule, 76 Fed. Reg. at 77731.

<sup>13</sup> Specifically, the Commission may only decline to approve the submission if it is inconsistent or appears to be inconsistent with the CEA or the Commission's regulations. See Proposed Rule, 76 Fed. Reg. at 77731.

<sup>14</sup> See Letter from Markit to the Commission, 3 (March 8, 2011).

<sup>15</sup> See Proposed Rule, 76 Fed. Reg. at 77737-38 (to be codified at 17 C.F.R. §§ 37.10(b), 38.12(b)).

<sup>16</sup> See 17 C.F.R. § 40.6(b).

<sup>17</sup> At the Open Meeting where the Commission considered the Proposed Rule, Chairman Gensler asked the Commission staff whether a SEF or DCM submitting a swap for an MAT Determination could make one submission for that type of swap or whether it would have to make 365 individual submissions to account for every potential effective date of the year. Staff responded that under the Proposed Rule, a SEF or DCM could submit an analysis for several different swaps in one submission but indicated that the rule does not contemplate making a single submission for a class or group of similar swaps. See Transcript of Open Meeting

February 13, 2012

Page 6

days will be sufficient time for the Commission to make an adequate review of MAT Determinations. In order to avoid Rule 40.6 from becoming a “rubber-stamp” for MAT Determinations, we urge the Commission to provide a 90 days review period including a provision for public comment to ensure that there is adequate time to review and approve MAT Determinations.

We believe these benefits would also likely be achieved if the Commission were to delegate the authority to make ultimate MAT Determinations to a third party such as the National Futures Association.

\* \* \* \* \*

We appreciate the opportunity to provide these comments on the Proposed Rule.

We thank the Commission for considering our comments. In the event you may have any questions, please do not hesitate to contact the undersigned or Marcus Schüler at [marcus.schueler@markit.com](mailto:marcus.schueler@markit.com).

Sincerely,



Kevin Gould  
President  
Markit North America, Inc.

---

On Two Final Rule Proposals Under The Dodd-Frank Wall Street Reform And Consumer Protection Act, dated Dec. 5, 2011 at 130-33.