From: Douglas Friedman <Douglas.Friedman@tradeweb.com>
Sent: Monday, December 6, 2010 12:09 PM
To: SEFRules <SEFRules@CFTC.gov>
Cc: Lee Olesky <Lee.Olesky@tradeweb.com>; Simon Hylson-Smith <Simon.Hylson-Smith@tradeweb.com>
Subject: Tradeweb Comment Letter re SEFs for the Pre-Comment Period
Attach: Tradeweb Comment Letter on SEFs.pdf

Attached please find Tradeweb's comment letter regarding SEFs in connection with the pre-comment period.

Please do not hesitate to contact me if you have any questions.

Best regards,

Doug

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Mr. David A. Stawick
Secretary to the Commission
Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Ms. Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609

Re: ***Swap Execution Facilities***

Dear Mr. Stawick and Ms. Murphy:

Tradeweb Markets LLC ("Tradeweb") appreciates the opportunity to provide comments to the Commodity Futures Trading Commission ("CFTC") and Securities and Exchange Commission ("SEC") (collectively, the "Commissions") with respect to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), and in particular, the definition of Swap Execution Facility ("SEF") and related Core Principles for SEFs in advance of the Commissions' proposed rulemaking on SEFs.[1]

Since 1998, Tradeweb has been at the forefront of creating electronic trading solutions which support price transparency and reduce systemic risk, the hallmarks of Title VII of the Dodd-Frank Act, and Tradeweb is broadly supportive of the Dodd-Frank Act and its stated goals. The Dodd-Frank Act recognizes the existence and importance of electronic execution facilities in achieving these objectives, and by distinguishing between SEFs and exchanges ("DCMs"), the Dodd-Frank Act further recognizes that both SEFs and DCMs can achieve these goals. The SEF definitions and associated core principles are largely adopted from exchange principles but that should not mean that the sole means through which swaps can and should be traded are exchanges. Indeed, if interpreted too narrowly, the rules could force existing electronic trading venues like Tradeweb to unnecessarily change their currently regulated platform's derivatives trading model -- from request for quote ("RFQ") to a central limit order book – even though Tradeweb's current RFQ model provides the electronic pre-trade transparency (through streaming prices), efficiency, liquidity, and risk reduction that the Dodd-Frank Act seeks to achieve.[2]

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[1] Tradeweb's comments are intended to address the definition and purpose of SEFs in connection with the pre-rule comment period. Tradeweb intends to submit comments to the proposed rules on SEFs once released, and Tradeweb has already submitted comments letters to the Commissions' proposed rules on mitigation of conflicts of interest, and intends to comment separately on the recently proposed rules on real-time trade reporting.

[2] Electronic RFQ is a fully-disclosed trading protocol, in which the liquidity taker (the client) can request (and receive) multiple, competitive prices (streaming, if requested) simultaneously; the liquidity makers (dealers) are aware of their identities before a trade is executed, and have discretion as to whether to respond and/or trade with such counterparties. The trades are completed for the full size (i.e., no partial fills).

We believe regulation should foster the benefits these platforms provide, rather than inhibit them, and the rules should create a competitive marketplace that encourages the provision of adequate liquidity to market participants. To that end, the rules should be flexible to include various trading models and protocols (e.g., RFQ, central limit order book, hybrid) so that the marketplace has access to trade in a manner consistent with the provision of liquidity and management of risk. The new rules for derivatives need to recognize the market characteristics and the important role of various trading models and protocols, not for the sake of private enterprise, but so that genuine end-users retain the flexibility and access to liquidity to effectively manage their risk.

In short, we are supportive of the goals to reform the derivatives markets and indeed we provide the very solutions the regulation seeks to achieve, but are concerned that the Commissions may overreach in their interpretation of the letter and spirit of the law, and in doing so create unintended consequences for end-users and the marketplace as a whole.

I. Background on Tradeweb

Tradeweb is a leading global provider of electronic trading platforms and related data services for the OTC fixed income and derivatives marketplaces. Tradeweb operates three separate electronic trading platforms: (i) a global electronic multi-dealer to institutional customer platform through which institutional investors access market information, request bids and offers, and effect transactions with, dealers that are active market makers in fixed income securities and derivatives, (ii) an inter-dealer platform, called Dealerweb, for U.S. Government bonds and mortgage securities, and (iii) a platform for retail-sized fixed income securities.[3]

Founded as a multi-dealer online marketplace for U.S. Treasury securities in 1998, Tradeweb has been a pioneer in providing market data, electronic trading and trade processing in OTC marketplaces for over 10 years, and has offered electronic trading in OTC derivatives on its institutional dealer-to-customer platform since 2005. Active in 20 global fixed income, money market and derivatives markets, with an average daily trading volume of $250 billion, Tradeweb's leading institutional dealer-to-customer platform enables more than 2,000 institutional buy-side clients to access liquidity from more than 40 sell-side liquidity providers by putting the dealers in real-time competition for client business in a fully-disclosed auction process. These buy-side clients comprise the majority of the world's leading asset managers, pension funds, and insurance companies, as well as most of the major central banks.

Since the launch of interest rate swap ("IRS") trading in 2005, the notional amount of interest rate derivatives traded on Tradeweb has exceeded $5 trillion from more than 65,000

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[3] Tradeweb operates the dealer-to-customer and odd-lot platforms through its registered broker-dealer, Tradeweb LLC, which is also registered as an alternative trading system ("ATS") under Regulation ATS promulgated by the SEC under the Securities Exchange Act of 1934. Tradeweb operates its inter-dealer platform through its subsidiary, Hilliard Farber & Co., Inc., which is also a registered broker-dealer and operates Dealerweb as an ATS. In Europe, Tradeweb offers its institutional dealer-to-customer platform through Tradeweb Europe Limited, which is authorized and regulated by the UK Financial Services Authority as an investment firm with permission to operate as a Multilateral Trading Facility. In addition, Tradeweb Europe Limited has registered branch offices in Hong Kong, Singapore and Japan and holds an exemption from registration in Australia.

trades. Tradeweb has spent the last 5 years building on its derivatives functionality to enhance real-time execution, provide greater price transparency and reduce operational risk. Today, the Tradeweb system provides its institutional clients with the ability to (i) view live, real-time IRS (in 6 currencies, including U.S., Euro, Sterling, Yen), and Credit Default Swap Indices (CDX and iTraxx) prices from swap dealers throughout the day; (ii) participate in live, competitive auctions with multiple dealers at the same time, and execute an array of trade types (*e.g.*, outrights, spread trades, or rates switches); and (iii) automate their entire workflow with integration to Tradeweb so that trades can be processed in real-time from Tradeweb to customers' middle and back offices, to third-party affirmation services like Markitwire and DTCC Deriv/SERV, and to all the major derivatives clearing organizations. Indeed, last month, Tradeweb served as the execution facility for the first fully electronic dealer-to-customer interest rate swap trade to be cleared in the U.S. Tradeweb's existing technology maintains a permanent audit trail of the millisecond-by-millisecond details of each trade negotiation and all completed transactions, and allows parties (and will allow SDRs) to receive trade details and access post-trade affirmation and clearing venues.

With such tools and functionality in place, Tradeweb is providing the OTC marketplace with a front-end swap execution facility. Moreover, given that it has the benefit of offering electronic trading solutions to the buy-side and sell-side, Tradeweb believes that it can provide the Commissions with a unique and valuable perspective on the proposed rules.

II. Background on the OTC Credit and Rates Derivatives Marketplace

How do the OTC credit and rates derivatives marketplaces operate today?

Today, there are generally two institutional marketplaces for over-the-counter (OTC) credit and rates derivatives: the dealer-to-customer market (institutional) and the interdealer market (wholesale). In the institutional market, the largest dealers buy and sell derivatives with their institutional customers (*e.g.*, asset managers, corporations, pension funds, *etc.*) on a fully-disclosed and principal basis. In the institutional market, the provision of liquidity is essential for corporations, municipalities and government organizations (*i.e.*, end users), which have numerous different asset and liability profiles to manage. The need for customized risk management solutions has led to a market that relies on flexibility – so end-users can adequately hedge interest rate exposure – and liquidity providers, who have the ability to absorb the varied risk profiles of end-users by trading standard and customized derivatives. These dealers then often look to the wholesale market – the market wherein dealers trade derivatives with one another – to obtain liquidity or offset risk as a result of transactions effected in the institutional market or simply to hedge the risk in their portfolios.

In the wholesale market, brokers ("IDBs") act as intermediaries working to facilitate transactions between dealers. There is no centralized exchange (i.e., derivatives are traded over-the-counter), and as a result, dealers look to IDBs to obtain information and liquidity while at the same time preserving anonymity in their trades. Currently, in the United States, these trades are primarily accomplished bilaterally through voice brokering. By providing a service through which the largest and most active dealers can trade anonymously, IDBs prevent other dealers from discerning a particular dealer's trading strategies, which in turn (i) reduces the costs

associated with the market knowing a particular dealer is looking to buy or sell a certain quantity of derivatives, (ii) allows the dealer to buy or sell derivatives in varying sizes, providing stability to the marketplace, and (iii) enhances liquidity in the marketplace.

Both the wholesale and institutional derivatives markets trade primarily through bilateral voice trading, with less than 5% of the institutional business trading electronically. In these markets, trades are often booked manually into back office systems and trades are confirmed manually (by fax or other writing), and some (but not all) derivatives trades are cleared.

How will (and should) the credit and rates derivatives markets operate under the Dodd-Frank Act?

With the implementation of the Dodd-Frank Act, we expect most of the derivatives market will be subject to mandatory clearing, traded on a regulated swap market, and the entire market will be subject to public reporting. Accordingly, with increased electronic trading, the credit and rates derivatives markets will be much more transparent and efficient, and systemic risk will be reduced as the regulated swaps markets establish direct links to designated clearing organizations ("DCOs") and swap data repositories ("SDRs").

In light of the foregoing and with the forthcoming business conduct standards, we believe the trading mandate was not intended to be and does not need to be limited to a specific trading model (*e.g.*, only anonymous central limit order book trading) to achieve the goals of the Dodd-Frank Act. Indeed, to do so, would undermine these goals. Requiring (directly or indirectly) central limit order book-like trading would materially impact current market structure, because it will likely reduce the number of instruments traded, and effectively reduce the ability for end-users to adequately manage their risk. In short, the move to a regulated electronic swap market (without regard to trading model but with the appropriate transparency and regulatory oversight) and clearing is what will accomplish the policy goals without hurting liquidity and disrupting the market. It is critical that the Commissions do not propose rules that artificially and unnecessarily hurt the market and undermine the goals of the Dodd-Frank Act.

III. Key Considerations for SEF Rulemaking

What is a SEF?[4]

While the definition of a SEF has been the subject of much debate and speculation, one thing is clear -- the Commissions should not read/interpret the SEF definition merely as a central limit order book because that would be redundant of the concept of exchanges/DCMs in the legislation. Indeed, we believe the plain language of the Dodd-Frank Act requires the

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[4] The term 'swap execution facility' has been defined in the Dodd-Frank Act 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- (A) facilitates the execution of swaps between persons; and (B) is not a designated contract market. The Dodd-Frank Act amends Section 1a of the Commodities Exchange Act with a new paragraph (50, and Section 761(a)(6) of the Dodd-Frank Act amends Section 3(a) of the Securities Exchange Act of 1934 by adding a new paragraph (77) (defining a "security-based swap execution facility"). We refer to both as a SEF in this letter.

Commissions to recognize the distinction between SEF's and DCM's, and particularly in light of the current working market structure and manner in which OTC derivatives trade (see discussion above), the Commissions should recognize trading models other than pure exchange.[5] Accordingly, it is critical that the Commissions do not impose requirements on SEFs that effectively make them exchanges – without expressly calling them exchanges. For example, if the Commissions were to propose rules that in order for a SEF to satisfy its pre-trade transparency requirement, all of its participants must be able to view (even if they cannot participate in) an ongoing RFQ negotiation, such disclosure might force the liquidity provider to widen its bid/offer spread so as to price in the risk associated with the information on that trade being broadcast to the entire market. It is not clear what the benefit of this would be to market participants.

What should a SEF be?

Consistent with the goals of the Dodd-Frank Act, for institutional users, a SEF should (i) provide pre-trade price transparency (e.g., through streaming prices for standardized transactions and competitive real time quotes for larger or more customized transactions), (ii) incorporate a facility through which multiple participants can trade with each other (i.e., must have competition among liquidity providers), (iii) have objective standards for participation that maintain the structure of liquidity providers (like swap dealers) providing liquidity to liquidity takers (institutional buy-side clients), (iv) have the ability to adhere to the core principles that are determined to be applicable to SEFs, (v) provide access to a broad range of participants in the OTC derivatives market, allowing such participants to have access to trades with a broad range of dealers and a broad range of DCOs; (vi) allow for equal and fair access to all the DCOs and allow market participants the choice of DCO on a per trade basis, and (vii) have direct connectivity to all the SDRs. A SEF does not need to be an exchange to meet this standards.

Why is RFQ an acceptable model for SEFs?

The electronic RFQ model is an acceptable model for SEFs because it gives multiple participants the ability to execute or trade swaps with multiple participants by allowing liquidity takers (clients) to access real-time electronic streaming of live, firm prices from multiple liquidity providers, or individually request real-time quotes from multiple liquidity providers. For example, for trades that are of a size or nature where streaming prices are not available or practicable, RFQ offers a client the ability to request a quote that will only be transmitted to the those liquidity providers selected by the client. This provides the buy-side client with access to multiple counterparty pricing, but limits the number of people in the market who know its trade -- thereby giving those liquidity providers in the RFQ sufficient time to redistribute the risk without other market participants interfering. Moreover, under the Dodd-Frank Act, the results

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[5] For an excellent statutory analysis and interpretation of the SEF definition, we refer to the Commissions to (a) pages 4-6 of Morgan Stanley's November 4, 2010 letter regarding the Definition of Swap Execution Facility, (b) International Swaps and Derivatives Association, Inc.'s (ISDA's) October 1, 201010 letter on the definition of Swap Execution Facility, and (c) the Asset Management Group (AMG) of the Securities Industry and Financial Markets Association (SIFMA) letter, dated November 24, 2010, each of which has been submitted during the Commissions' pre-comment period for SEF rulemaking.

of these transactions will be reported in real-time and publicly disseminated, thus enhancing transparency in the market.

What are the key concerns regarding the Core Principles applicable to SEFs?

In order to register and operate as a SEF, the "trading system or platform" must comply with the enumerated Core Principles in the Dodd-Frank Act applicable to SEFs. Regulators have the authority to determine the manner in which a SEF complies with the statutory core principles, and there is discretion for the Commissions to retain distinct regulatory characteristics for SEFs versus DCMs. It is critically important for the Commissions to apply the principles with flexibility given the market structure in which swaps are traded. Accordingly, regulators should interpret core principles in a way in which SEF's can actually comply with them. While many of the SEF Core Principles are broad, principle-based concepts -- which make sense given the potential for different types of SEFs and trading models – some of the Core Principles are potentially problematic for SEFs that do not operate a central limit order book or clearing. For example, the *Position Limits or Accountability* Core Principle continues to be a big issue in terms of a SEF's ability to know and react to the parties' positions (i.e., each SEF will need a full market view to have the appropriate transparency to monitor this issue). This would require cooperation among all the venues (SEFs, DCMs and DCOs), including position information sharing agreements, so that if a position was exceeded, the SEF could block any execution. In turn, in order to comply with and enforce the *Emergency Authority* Core Principle, SEFs will need the ability to establish clear rules and guidelines about communication and coordination with the Commissions (i.e., when SEF can invoke emergency authority and the notice requirements related thereto), and the ability for positions to be liquidated through the regulated swaps market, which is typically not part of the platform's role.

It is imperative that the Commissions do not interpret the SEF Core Principles to require a SEF to act like an exchange – that is what the DCM core principles are designed to do.

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In sum, while we are supportive of the goals of the Dodd-Frank Act and believe increased regulatory oversight is good for the derivatives market, we want to emphasize that flexibility in trading models for execution platforms are critically important to maintain so end-users can manage their risks in a flexible manner. If you have any questions concerning our comments, please feel free to contact us. We welcome the opportunity to discuss these issues further with the Commissions and their staff.

Sincerely,

Lee H. Olesky
Chief Executive Officer

Douglas L. Friedman
General Counsel