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Swap Execution Facility (SEF) discussion

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A Swap Execution Facility (SEF) should:

Support deep and liquid markets by providing

- · Bids and offers via multiple venues, such as many-to-many, voice, and electronic execution platforms
- Pricing for standardized cleared swaps that are representative of the more liquid parts of the swap market
- · Pricing data (bids/asks) to all market participants at the same frequency at no additional cost
- · Client anonymity unless the client chooses otherwise in order to request for quote (RFQ) due to liquidity constraints

Support an RFQ model, which helps facilitate best execution for investors and

- · Helps achieve best execution for large size trades, for trades for less liquid assets, and in times of market distress
- Supports an open selection market where the requestor of quote is allowed to direct their inquiry to any provider
- Supports market liquidity by allowing liquidity providers to transfer risk, which helps the pricing provided clients
- There is concern that if the RFQ model is not available, liquidity risk will transition from the liquidity provider to the investor

Support operational and cost efficiency by offering

- The ability to execute block trades and then allocate trades at the fund level
 - FCM selection is at the fund level
 - CCP selection is at the fund level
- · Operational flows with straight-through-processing and minimum manual touch points

Have a governance structure with appropriate representation from the investor community that

- Governs who is allowed to conduct business on the SEF
- Is based on an open architecture system that allows connectivity if the entity meets selection criteria

Support efficient functional structure by

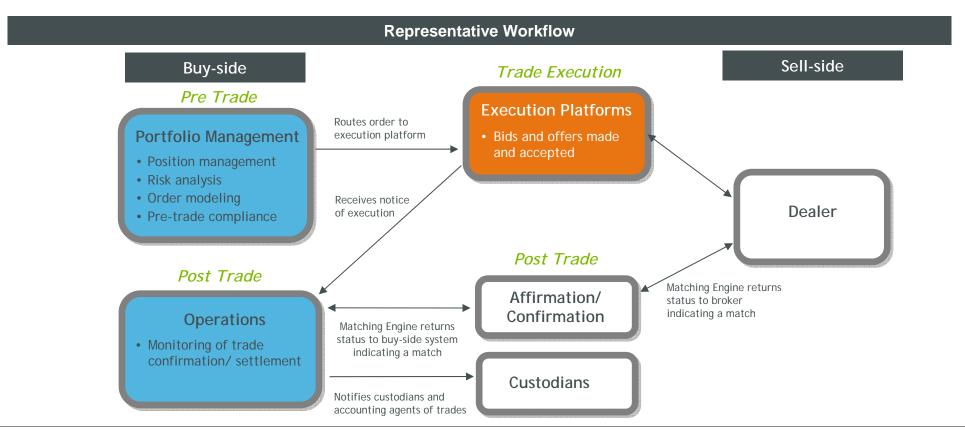
· Keeping clear accountability of market risk ownership until accepted for clearing

II. Buy-Side Investment Process

Buy-side participants need their own systems and processes to track, reconcile and manage each aspect of the investment process

- · Maintain each portfolio's positions, risk analytics, compliance requirements
- Help construct portfolios
- Model and manage orders (including routing them to execution venues)
- Capture trades once executed (including receiving back executions)
- All post-execution operations

Buy-side post-trade process is fundamentally different from sell-side process as it is much more operationally intensive



Many Players Involved in Swap Transaction Processing

Hundreds of companies including operations outsourcing providers, accounting agents, custodians, technology vendors, risk management vendors help process swaps without execution or trading

Accounting Systems

- Track and reconcile positions
- Calculate prices
- Compute and reconcile cash flows (P&I)

Operational Systems

- Track and reconcile positions
- Calculate prices
- Manage collateral
- Compute and reconcile cash flows (P&I)

Execution Platforms

• Where buyers and sellers come together to execute trades

Risk Systems

- Track positions
- Calculate prices and analytics
- Compute cash flows (P&I)

Portfolio Management Systems

- Track positions
- Compute and display cash flows (P&I)
- Calculate prices and analytics

Affirmation/Confirmation

- Allow buy-side and sell-side participants to submit trades for matching
- Help facilitate and manage portfolio breakdown/allocation
 process

Interpretation of SEF Definition Under Dodd-Frank

Definitional section (§ 721) clearly states that a SEF involves execution or trading of swaps:

"[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 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."

However the registration section (§ 733) requires any entity that operates a facility for trading or processing of swaps to register as a SEF:

• "No person shall operate a facility for the *trading or processing of swaps* unless the facility is registered as a swap execution facility or as a designated contract market."

"Processing" is fundamentally different from "execution":

Execution	Processing
 Facilitates swap execution and sends for processing 	 Allows client to keep its own version of transaction
 Promotes pre-trade price transparency Assumes counterparty risk Where buyers and sellers come together to execute trades - a marketplace 	 Supports post-execution reconciliations and operations Where operations and reconciliations are performed - a clients' books & records

As stated by Congress, the goal is to:

"promote the trading of swaps on swap execution facilities and to promote pretrade price transparency in the swap markets"

Consistent with section (§ 721), BlackRock recommends processing systems that do not perform execution not be required to register as SEFs. Otherwise, there may be unintended consequences that include:

- Potentially hundreds of accounting, portfolio management, operations and other systems not directly involved with trade execution are captured as SEFs
- Hundreds of registered SEFs, coupled with ownership restrictions, will create significant complexity and confusion in the marketplace

III. Swap Data Repositories (SDRs)

Fund level reporting and timing

- Ultimate reporting at fund allocation level (legal ownership)
- · Timeline needs to respect that fund allocations need to be reset to actual fill quantities
- Supports transparency yet avoids leakage of information

Potential entities for reporting

- · Entities that could provide consistent data in a single format across the market
 - For cleared OTC derivative trades, CCPs
 - · Have the tools and risk management expertise
 - Are known counterparts to all trades
 - · Can provide risk-based aggregation for systemic risk concerns
 - · Minimize the risk of double counting trades
 - For bilateral swaps (uncleared), DTCC
 - Is a central repository for majority of legal confirms
 - For exchange-traded products, Exchanges

Time stamp

- For pre-enactment trades, the time stamp should be a set time of day of the enactment of the bill
- For post-enactment trades, the time stamp should be when trade is accepted for clearing (for cleared trades) or affirmed at the fund level (for uncleared trades)

