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March 2, 2020

Mr. Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Re: *Post-Trade Name Give-Up on Swap Execution Facilities (RIN 3038-AE79)*

Dear Mr. Kirkpatrick:

The Investment Company Institute (ICI)¹ appreciates the opportunity to provide comments to the Commodity Futures Trading Commission (CFTC or “Commission”) on its proposed rulemaking to prohibit post-trade name give-up for certain swaps (“Proposed Rule”).² Under the practice of post-trade name give-up, the identity of each swap counterparty is disclosed to the other after a trade has been matched anonymously on a swap execution facility (SEF). The Proposed Rule would prohibit this practice for swaps that are executed anonymously on SEFs and are intended to be cleared (“Covered Swaps”).

For the reasons explained below, we strongly support the CFTC’s proposal to prohibit post-trade name give-up for Covered Swaps. The current practice is unnecessary, and harms regulated funds and their shareholders. By adopting the proposed prohibition, the CFTC would further the Congressional goals of promoting liquidity, fairness, and competition on SEFs.³

¹ ICI is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI’s members manage total assets of US\$25.2 trillion in the United States, serving more than 100 million US shareholders, and US\$7.7 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

² *Post-Trade Name Give-Up on Swap Execution Facilities*, 84 Fed. Reg. 72262 (Dec. 31, 2019), available at <https://www.govinfo.gov/content/pkg/FR-2019-12-31/pdf/2019-27895.pdf> (“Proposing Release”).

³ In the Commodity Exchange Act (CEA), Congress calls for the promotion of:
(i) the trading of swaps on SEFs and pre-trade price transparency in the swaps market;
(ii) the public interest served by swap trading in liquid, fair and financially secure trading facilities; and
(iii) responsible innovation and fair competition among SEFs and swap market participants. See §§ 5h(e) and 3 of the CEA.

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Background

US registered investment companies, including mutual funds, ETFs, and other funds that are regulated under the Investment Company Act of 1940 (“registered funds”), and non-US regulated funds⁴ (together with registered funds, “regulated funds”) rely on their investment adviser to invest fund assets and implement the funds’ investment objectives and strategies. A regulated fund’s investment adviser employs portfolio managers and traders to carry out these functions on behalf of the fund. In managing a regulated fund’s portfolio, the portfolio manager determines which assets to buy or sell for the fund, in accordance with the objectives described in the fund’s prospectus. Traders seek to execute the transactions in the most efficient and cost-effective manner to effectuate the investment strategy. Importantly, a regulated fund’s investment adviser is a fiduciary and owes duties of loyalty and care to its clients, including the regulated funds it manages. This fiduciary duty obligates the adviser, including its portfolio managers and traders, to act in the best interest of the fund and to seek best execution of the fund’s portfolio transactions.

Investment advisers use derivatives in a variety of ways on behalf of regulated funds. Derivatives are a particularly useful portfolio management tool in that they offer portfolio managers considerable flexibility in structuring the investment portfolios of regulated funds. For example, a portfolio manager may use derivatives to hedge a regulated fund’s positions, equitize the regulated fund’s cash that it cannot immediately invest in direct equity holdings, manage the regulated fund’s cash positions, and adjust portfolio duration, all in accordance with the investment objectives stated in the fund’s prospectus.

Investment advisers use SEFs to enter into swaps on behalf of their clients, including regulated funds. These swaps include swaps that are subject to the trade execution requirement (and thus must be traded on or subject to the rules of a SEF or designated contract market) as well as swaps that investment advisers choose to execute through a SEF rather than bilaterally. ICI and its members therefore have a strong interest in the regulation of SEFs and of SEF trading practices.

Post-Trade Name Give-Up Is Unnecessary for Intended to Be Cleared Swap Trades

For uncleared swaps, counterparty identity is an important consideration because each party to the swap is exposed to the credit risk of its counterparty for the duration of the swap. Each party to the swap also needs to know the identity of its counterparty to monitor credit exposure and payment obligations that the party may owe to, or be owed by, its swap counterparty.

⁴ For purposes of this letter, the term “non-US regulated fund” refers to any fund that is organized or formed outside the United States, is authorized for public sale in the country in which it is organized or formed, and is regulated as a public investment company under the laws of that country. For example, UCITS, or “undertakings for collective investment in transferrable securities,” are collective investment schemes established and authorized under a harmonized European Union (EU) legal framework, currently EU Directive 2009/65/EC, as amended (UCITS IV).

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By contrast, for a Covered Swap, clearing obviates the need for market participants to know the identity of their counterparties for credit risk, legal, or operational purposes. A Covered Swap executed on a SEF is extinguished as soon as it is accepted by a Derivatives Clearing Organization (DCO) for clearing. The extinguished swap is then replaced by two equal and opposite swaps. The buyer of the extinguished swap becomes the buyer of one of the two new swaps, with the DCO acting as the seller of such swap. The seller of the extinguished swap becomes the seller of the other new swap, with the DCO acting as the buyer of such swap. Neither counterparty to the Covered Swap is exposed to the credit risk of the other counterparty to that extinguished swap. And, because the swap is extinguished upon acceptance for clearing, the original parties to the Covered Swap have no ongoing payment obligations to the other on that transaction. Thus, there is no reason either party to a Covered Swap needs to know the identity of its counterparty.

With respect to any concerns regarding credit risk before the Covered Swap is extinguished, applicable pre-execution credit checks and straight-through processing requirements effectively eliminate such counterparty risk as well as the need for market participants to know the identities of the counterparties to the Covered Swap.

Post-Trade Name Give-Up Is Harmful to Market Participants

Post-trade name give-up institutionalizes a form of information leakage that results in less favorable trading conditions for buy-side market participants, including regulated funds and their shareholders. For example, disclosure of the identity of a regulated fund as a dealer's swap counterparty provides the dealer with information about the fund's trading intentions, positions, strategies, and other sensitive information that can be used to the dealer's advantage. Leaking this sensitive information through post-trade name give-up harms funds and their shareholders both directly (by increasing trading costs) and indirectly (by disclosing real-time information about the fund's holdings, strategies and trading interest). This leaked information can help a dealer anticipate its client's future trading behavior and potentially cause the dealer to offer the client less favorable pricing and other terms for swaps that are entered into bilaterally.

Post-trade name give-up is especially problematic for regulated funds and their shareholders. As noted above, advisers to regulated funds are fiduciaries. Traders employed by the adviser must seek best execution for the fund's transactions, which involves seeking the best price available while minimizing the market impact of the transaction. But the market impact of a trade will increase if information about the trade leaks into the market through post-trade name give-up, allowing other market participants to anticipate future trading intentions.

Unfortunately, buy-side traders have limited tools to reduce harms associated with the information leakage that accompanies post-trade name give-up. An effective way to prevent these harms is to conduct extensive due diligence on potential trading venues and avoid using venues that require post-trade name give-up of Covered Swaps. Thus, SEFs' use of post-trade name give-up acts as an impediment to greater SEF participation by buy-side participants, including advisers to regulated funds.

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As the Commission acknowledged, information leakage through post-trade name give-up also is inconsistent with the information privacy requirements that Congress set up for swap data repositories (SDRs).⁵ Specifically, CEA section 21(c)(6) provides that an SDR must “maintain the privacy of any and all swap transaction information that the swap data repository receives from a swap dealer, counterparty, or any other registered entity [including a SEF].”⁶ CFTC Regulation 49.17(f)(2), which implements this requirement, provides that for Covered Swaps, the swap data and information maintained by the SDR may be accessed by either party to the particular swap *except for* the identity of the counterparty or the counterparty’s clearing member for the swap.⁷ Yet, under the current practice of post-trade name give-up, the party can still obtain the identity of its counterparty—thereby undermining the purpose of § 49.17(f)(2) and rendering meaningless the SDR information privacy requirements for Covered Swaps.

We also agree with the Commission that the practice of post-trade name give-up may have a discriminatory effect on certain market participants, deterring them from joining or trading in a meaningful way on SEFs. As the Commission noted, a trading practice that results in such discrimination undermines the goals of the impartial access requirement under CEA section 5h(f)(2)(B).⁸

Prohibiting Post-Trade Name Give-Up Would Increase Liquidity on SEFs by Encouraging Buy-Side Participants to Trade More Swaps on SEFs

Post-trade name give-up reduces liquidity and results in more fragmented swap markets. If the Commission prohibits the practice of post-trade name give-up, buy-side traders would be more likely to participate in trading on venues that offer anonymous execution of intended to be cleared swaps, including venues that offer order book functionality.

Some advocates of post-trade name give-up have argued that prohibiting this practice would not lead to increased liquidity because some SEFs currently offer fully anonymous order books without post-trade name give-up on a “dealer-to-client” basis and participation in these order books has been very limited. Limited participation today in fully anonymous order books on some SEFs, however, is not a meaningful indicator of whether prohibiting post-trade name give-up would lead to increased liquidity in the future on SEFs overall. As explained above, regardless of where SEF liquidity is concentrated today, prohibiting post-trade name give-up (and thereby providing the ability to trade fully anonymously for all methods of execution) would attract more buy-side participants to trade on SEFs.

⁵ See Proposing Release at 72266.

⁶ 7 U.S.C. § 24a(c)(6).

⁷ See 17 C.F.R. § 49.17(f)(2). The CFTC SDR information privacy requirement applies to both reporting and non-reporting parties.

⁸ See Proposing Release at 72266-67.

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Advocates of post-trade name give-up have also argued that prohibiting post-trade name give-up may result in the reduction of aggregate liquidity and efficiency as dealers may be discouraged from trading on anonymous SEFs without post-trade name give-up. That outcome is unlikely, as dealers would have no reason to cut back on their business simply because they can no longer obtain information about buy-side swap counterparties. To the contrary, prohibiting post-trade name give-up could encourage competition among dealers to the extent post-trade name give-up today gives a few dominant dealers in the market leverage over buy-side participants and other dealers.

Other Arguments for Retaining Post-Trade Name Give-Up Lack Merit

Some advocates of post-trade name give-up have suggested that the practice should be preserved to allow banks to allocate their bank capital among their preferred customer base and that banks, if unable to so allocate their capital, would charge higher prices to all customers. We do not believe this is a compelling reason to retain post-trade name give-up. Further, a practice by banks of only entering into swaps with counterparties that are preferred customers does not promote liquidity, fairness, or competition.

Advocates of post-trade name give-up also have suggested that the identity of a buy-side participant is needed to deter participants from gaming the market. The concern appears to be that, if counterparties can trade anonymously on a SEF, they might engage in trading practices that undermine market integrity. We view this concern as misguided and believe that post-trade name give-up is not the appropriate tool to address any regulatory concerns about trading practices. Rather, we agree with Chairman Tarbert, Commissioner Behnam, and Commissioner Berkovitz that existing CFTC and SEF rules regarding market conduct and trading practices appropriately address any such concerns.⁹

Scope of Prohibition

We believe that the prohibition on post-trade name give-up should extend to all Covered Swaps regardless of whether the swap is subject to the clearing or trade execution mandate. As explained above, post-trade name give-up is not only unnecessary, but also harmful to market participants that enter into swaps that are anonymously executed and intended to be cleared. A broad prohibition would more effectively further Congressional intent to promote trading on SEFs.¹⁰

At the same time, we support one possible exception for certain package trades. With respect to package trades that include (i) a swap that is intended to be cleared and (ii) a swap that will remain uncleared, each party will need to know the identity of its swap counterparty because of the uncleared leg of the transaction. Because each party to the package transaction is exposed to the credit risk of its counterparty for the duration of the uncleared leg(s), a blanket prohibition on post-trade name give-up

⁹ See Proposing Release at 72273, n.16 (Joint Statement of Chairman Heath Tarbert, Commissioner Rostin Behnam, and Commissioner Dan M. Berkovitz).

¹⁰ See *supra* note 3.

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for Covered Swap transactions that are components of package transactions would prevent parties to these transactions from performing necessary checks on their counterparties for the uncleared swap components. Thus, to the extent that such packages are traded anonymously, we believe that the Commission should not prohibit post-trade name give-up for those transactions.

This exception would be important to preserve the ability of market participants to engage in these package transactions. Today, individual swap transactions are often executed together as a package transaction (one economic transaction) either to achieve a specific risk profile or to manage the size of a given portfolio. Compared to individual executions of each component, package transactions have a number of economic benefits including (i) more efficient risk transfer and hedging by allowing counterparties to exchange only net risk, (ii) eliminating risk that the pricing will change between the execution of each leg, and (iii) lower transaction costs.

To promote clarity and consistency, we recommend that the CFTC use the same definition of “package transaction” for purposes of this rule as the definition it proposed to adopt in the recent SEF proposal.¹¹ That proposal defines a “package transaction” to mean a transaction that:

consists of two or more component transactions executed between two or more counterparties where: (i) At least one component transaction is subject to the trade execution requirement in section 2(h)(8) of the Act; (ii) Execution of each component transaction is contingent upon the execution of all other component transactions; and (iii) The component transactions are priced or quoted together as one economic transaction with simultaneous or near-simultaneous execution of all components.¹²

This proposed definition has been the working standard for years as a result of a number of staff no-action letters.¹³ The Commission also proposed a similar definition in its November 2018 proposal for amendments to SEF rules.¹⁴ We support this proposed definition and the Commission’s efforts to promote clarity and consistency for market participants.

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¹¹ *Swap Execution Facility Requirements and Real-Time Reporting Requirements*, 85 Fed. Reg. 9407 (Feb. 19, 2020), available at <https://www.cftc.gov/sites/default/files/2020/02/2020-02721a.pdf>

¹² CFTC Proposed Regulation 36.1(a)(1).

¹³ See, e.g., CFTC Letter 14-137 (Nov. 10, 2014) at 4, available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/14-137.pdf>; CFTC Letter 17-55 (Oct. 31, 2017), at n.2, available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/17-55.pdf>.

¹⁴ See *Swap Execution Facilities and Trade Execution Requirement*, 83 Fed. Reg. 61946, 62097 (Nov. 30, 2018) (proposed Regulation 37.201(b)(1)), available at <https://www.govinfo.gov/content/pkg/FR-2018-11-30/pdf/2018-24642.pdf>.

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We appreciate the opportunity to comment on the Proposed Rule and urge the Commission to adopt it promptly. If you have any questions on our comment letter, please feel free to contact me at (202) 326-5835.

Sincerely,

/s/ Sarah A. Bessin

Sarah A. Bessin
Associate General Counsel

cc: The Honorable Heath P. Tarbert
The Honorable Brian D. Quintenz
The Honorable Rostin Behnam
The Honorable Dawn DeBerry Stump
The Honorable Dan M. Berkovitz

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