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March 5, 2012

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: Registration and Regulation of SB Swap Execution Facilities, 76 FR 10948 (February 28, 2011)

Dear Ms. Murphy:

I appreciate the opportunity to provide the following comments to the Securities and Exchange Commission ("Commission") with respect to the proposed rules in the above-referenced release ("Release"). Proposed Regulation SB SEF is designed to create a framework for a security-based swap ("SB swap") execution facility ("SB SEF") under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank").

I. Trading Protocols: RFQ Interaction with Resting Orders

The Commission proposes that a SB SEF could meet Dodd-Frank pre-trade price transparency requirements for block trades by using a request-for-quote ("RFQ") platform" as long as the block trade interacts with existing interest on the SB SEF (*i.e.*, the limit order book portion of the SB SEF that handles orders that are not blocks)... ."[1] The Commission should not mandate RFQ transactions to interact with any existing limit order book interest on a SB SEF. Mandating restrictive SB SEF quote and trading protocols has the potential to adversely affect trading in SB swaps. In this case, imposing a trading protocol that could materially alter the size of a block trade would interject uncertainty for the liquidity provider responding to an RFQ.[2] Instead, liquidity seekers should be given the option of interacting with such quotes if it is consistent with their trading strategy. Further, the Commission should not underestimate the increased costs associated with mandating RFQ transactions interacting with a limit order book. Such a protocol will significantly increase the possibility of splitting a transaction into multiple executions resulting in increased allocations, associated back-office burdens and settlement complexities. These costs will ultimately be borne by market participants and end-users.

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[1] Release p. 10974. The Release is ambiguous as to whether non-block RFQ transactions would also be required to interact with existing interest on a SB SEF. We ask the Commission to provide clarification to the extent that it adopts final rules requiring such interaction.

[2] Liquidity providers responding to a block trade RFQ factor in the size of the trade when quoting a price as it is a key variable in the "negotiation process."

II. Proposed Financial Disclosure Requirements

SB SEFs are required to have adequate financial, operational, and managerial resources to discharge each responsibility of the SB SEF.[3] More specifically a SB SEF's financial resources are considered to be adequate if those resources enable the SB SEF to "(i) ... meet its financial obligations to its members and participants notwithstanding a default by the member or participant creating the largest financial exposure for that organization in extreme but plausible market conditions; and (ii) exceeds the total amount that would enable the SB SEF to cover the operating costs of the SB SEF for a one year period, as calculated on a rolling basis."[4] In order to evidence its financial resources a SB SEF and, in some cases its affiliate, are required to provide a complete set of financial statements to the Commission in support of its application.[5] The Commission proposes that financial information submitted pursuant to the proposed SB SEF rules would not necessarily be deemed confidential and would be publicly available unless the Commission granted confidential treatment under the Freedom of Information Act ("FOIA").[6]

The financial strength of an affiliate should not be a factor in determining the financial strength of an SB SEF. A SB SEF must comply with applicable rules and maintain necessary financial recourses regardless of the financial condition of the parent. Where a parent does not exercise day-to-day control over a SB SEF and a SB SEF can evidence that it is sufficiently capitalized, there is no need to look to the financial health of a parent. This is especially true where a SB SEF assumes no counter-party risk, takes no proprietary positions and, by its design and operation, is not responsible for any clearing or credit default by a market participant. One would observe that the Commodity Futures Trading Commission ("CFTC") does not propose to obligate a swap execution facility ("SEF") to submit its parent's financial statements.[7] Differing proposals on the same issue reflects a lack of coordination between the Commission and the CFTC in regulating the two markets. Such inconsistencies may create unnecessary barriers to entry for certain entities seeking to act as SB SEFs. In any event, all financial statements provided to the Commission in conjunction with a SB SEF application should be afforded confidential treatment and not be subject to FOIA disclosure requests.[8]

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[3] Section 3D(d)(12)(A) of the Securities Exchange Act of 1934 ("Exchange Act").

[4] Section 3D(d)(12)(B) of the Exchange Act.

[5] Exhibit H of proposed Form SB SEF would require the disclosure of unconsolidated financial statements for the applicant's affiliated entities including every subsidiary in which the applicant has, directly or indirectly, a 25% interest and for every entity that has, directly or indirectly, a 25% interest in the applicant. Release at 11069.

[6] 5 U.S.C. 522.

[7] See Core Principles and Other Requirements for Swap Execution Facilities, 76 FR 1214 (January 7, 2011) ("SEF Release").

[8] See Rule 17h-2T, Risk Assessment Reporting Requirements for Broker and Dealers. Under Rule 17h-2T a broker-dealer is required to provide the Commission with consolidated financial statements on itself as well as "associated persons" (*i.e.*, those persons whose "business activities are reasonably likely have a material impact on the financial and operational condition" of the broker-dealer). All information collected under Rule 17h-2T is deemed confidential and protected from FOIA disclosure. .

III. Third-Party Regulatory Services

It is essential for the Commission to recognize the ability of a SB SEF to use a third-party regulatory service provider to assist in complying with SB SEF Core Principles and related rules.[9] The ability of SB SEFs to broadly avail themselves of a third-party regulatory service provider would allow SB SEFs to cost-effectively meet compliance obligations and effective dates as well as allow them to more efficiently focus on integrating the new rules imposed on them. The Commission has recognized the appropriateness of regulatory outsourcing arrangements in other contexts.[10] The CFTC has also recognized the appropriateness of contracting for professional services and explicitly proposes that SEFs can use a third-party regulatory service provider for assistance in performing their SRO oversight functions.[11] Under such an arrangement the SB SEF would retain responsibility for complying with the Core Principles and related rules but would use a third-party to perform certain functions.[12] Moreover, entities seeking to be both a SB SEF and a SEF will not be able to capitalize on the opportunity afforded to them by the CFTC to use such third-party regulatory service provider if it has to "build" and staff its own compliance program in-house for essentially the same activity in the SB SEF environment. There exists a compelling need to harmonize the regulatory regimes of the Commission and the CFTC in this regard in order to avoid creating a barrier to entry that may ultimately reduce the number SB SEFs and decrease the competition among SB SEFs.

IV. International Harmonization

Dodd-Frank provides that no provision relevant to SB swaps "shall apply to any person insofar as such person transacts a business in security-based swaps without the jurisdiction of the United States, unless such person transacts such business in contravention of [Commission anti-evasion rules]."[13] The reach of Dodd-Frank could be very broad. The Commission has noted, for example, that if a U.S. person executes a SB swap anywhere in the world the information related to that SB swap should be reported in the United States because U.S. regulators have an interest in ensuring they have knowledge of the transaction.[14] The Commission has also stated that where a SB swap was executed in the United States it

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[9] Exhibit G of proposed Form SB SEF would require a SB SEF to provide executed copies of agreements entered into by the application including "third-party regulatory service" agreements. There is no further discussion or mention of the use of a third-party regulatory service provider in the Release.

[10] For example, Regulation ATS allows self-regulatory organization ("SRO") functions to be performed by a third-party entity. See Regulation of Exchanges and Alternative Trading Systems, 63 FR 70844, 70863 (December 22, 1998).

[11] Under the proposal the SEF maintains the ultimate obligation for compliance with the regulations. SEF Release at 1224.

[12] Regardless of the scope or nature of the functions outsourced, a SB SEF would retain exclusive authority over all substantive decisions made by its regulatory service provider.

[13] Section 772 of Dodd-Frank.

[14] Proposed Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information, 75 FR 75208, 75240 (December 2, 2010).

would be subject to U.S. jurisdiction even if the counterparties were not U.S. persons.[15]

The SB swaps marketplace is a global business. A large percentage of swap transactions involve non-U.S. banks as counterparties to U.S. persons. It is critically important for SB SEFs and market participants to have legal certainty about which entities and transactions are subject to U.S. regulation and which are not. This is particularly important as foreign regulators are developing their own regulatory rules and requirements for the OTC derivatives market. Harmonization of efforts among U.S. and foreign regulatory authorities in this regard is mission critical. Absent regulatory clarification and coordination a SB SEF could be required to have one set of rules for U.S. participants and another set of rules for non-U.S. participants with a further set of transaction-level rules (*i.e.*, based on the counterparties or underlying instruments). All of this would lead to market fragmentation and unnecessarily confusing, disparate rules and requirements. That undesirable situation could lead to unintended consequences, such as regulatory arbitrage, all of which would be at odds with the regulatory goals of Dodd-Frank and the financial interests of the United States.

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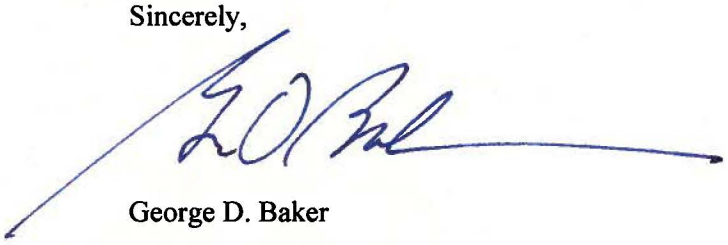
I appreciate the opportunity to provide these comments on the proposed rules.

Sincerely,



George D. Baker

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[15] Id.