

January 24, 2012

The Honorable Frank Lucas
Chairman
Committee on Agriculture
U.S. House of Representatives
2311 Rayburn House Office Building
Washington, DC 20515

The Honorable Collin Peterson
Ranking Member
Committee on Agriculture
U.S. House of Representatives
2211 Rayburn House Office Building
Washington, DC 20515

Re: H.R. 2586, the Swap Execution Facility Clarification Act

Dear Chairman Lucas and Ranking Member Peterson:

I am writing on behalf of the Investment Company Institute¹ to express support for H.R. 2586, the Swap Execution Facility Clarification Act, a bill to refine the definition of swap execution facility ("SEF") in Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). This bill would encourage migration of swap trading to the cleared and SEF-executed market.

Mutual funds and other registered investment companies (collectively, "funds") use swaps and other derivatives in a variety of ways. ICI and its members thus have a strong interest in ensuring that the new regulatory framework for the derivatives markets fulfills the objectives of the Dodd-Frank Act by supporting and fostering markets that are highly competitive, efficient, transparent and liquid. We are concerned that SEF-related proposals by the Commodity Futures Trading Commission's ("CFTC") and the Securities and Exchange Commission's (together, "Commissions") do not provide a sufficiently flexible execution framework to obtain these goals.²

ICI supports the provisions in the bill that limit the Commissions' ability to adopt overly prescriptive requirements for SEF trading systems or platforms. The structure of SEFs will decisively influence whether funds use SEFs, or some other vehicle, to interact with the derivatives markets. The appropriate regulation of SEFs will

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$12.47 trillion and serve over 90 million shareholders.

² See Statement for the Record of the Investment Company Institute, Hearing on "Emergence of Swap Execution Facilities: A Progress Report," Subcommittee on Securities, Insurance and Investment, Committee on Banking, Housing and Urban Affairs, U.S. Senate, July 29, 2011.

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be of critical importance to the success of the Title VII regulation and rulemaking. ICI believes that the proposed trading restrictions in the Commissions' SEF-related proposals do not strike the right balance. The proposed restrictions enhance transparency at the expense of liquidity and efficient pricing, which could discourage the use of SEFs. The bill should help to correct this problem by preserving SEFs' flexibility to develop execution frameworks that will attract market participants.

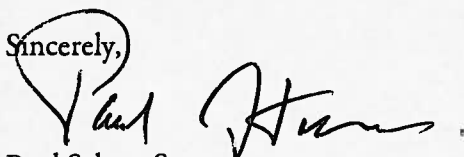
For example, one of the provisions in the Swap Execution Facility Clarification Act would prohibit the Commissions from requiring a SEF to have a minimum number of participants respond to any trading system or platform functionality. This provision speaks to the Commissions' proposals regarding the request for quote ("RFQ") process for the execution of swaps. ICI supports the Commissions' proposed use of RFQ systems but questions, for instance, the CFTC's proposal to require that an RFQ be sent to five or more dealers. If a fund is required to go to five swap dealers prior to executing a swap transaction, it likely would suffer from information leakage and "signaling" regarding the potential transaction, which would result in the market moving against the fund. Funds and their shareholders would bear the related costs in the form of a wider bid-ask price.

A second provision in the bill would prohibit the Commissions from requiring a SEF to mandate that bids or offers on one of the SEF's trading systems or platforms must interact with bids or offers on another of its trading systems or platforms. This provision would address components of the Commissions' proposals that would require market participants to interact with resting bids or offers. In the swaps market, forcing quotes to first interact with better priced existing bids and offers may result in several negative consequences. First, it nullifies the RFQ process and thereby hinders funds' execution strategies and objectives. Second, it fails to recognize that factors in addition to price must be considered when calculating the quality of a potential swap execution. Third, it results in fragmentation of orders, instead of a single execution, resulting in higher transaction, reporting and margin costs to be borne by funds and their shareholders. Each of these factors alone may discourage swap trading on SEFs.

As you know, funds participate in these markets on behalf of tens of millions of fund shareholders—Americans who invest through us to achieve their most important financial goals. On their behalf, we are keenly interested in ensuring that the emerging new regulatory requirements for the derivatives markets achieve legitimate policy objectives with minimal disruption to the markets, market participants, and their customers. Preserving the flexibility of SEF trading systems is one of the key steps along the way. We hope that you will keep our views in mind as you consider this legislation and otherwise oversee regulatory efforts to implement the Dodd-Frank Act.

With kindest regards.

Sincerely,



Paul Schott Stevens

President & CEO

Investment Company Institute