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April 22, 2016

David R. Pearl,
Office of the Executive Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC

RE: Notice Seeking Public Comment on the Evolution of the Treasury Market Structure

Dear Mr. Pearl:

On behalf of ICAP plc[1], we are pleased to provide our comments in response to the US Treasury's Request for Information regarding the evolution of the US Treasury Market Structure (the "RFI").[2]

We believe the U.S. Treasury market functions well in many respects, but there have certainly been significant developments in the market over the years and it is wholly appropriate for the official sector to explore how those developments have affected the market and whether any changes need to be made. The importance of the U.S. Treasury market to the U.S. economy and financial markets around the world cannot be overstated. Developments in the U.S. Treasury market determine the cost that the United States and its taxpayers can borrow funds, the prices that consumers pay for mortgages and other consumer loans, the cost for businesses to fund their activities, and the value of a wide range of other securities and financial products that are priced with reference to the U.S. Treasury market as a benchmark. It is imperative that the market be fair, transparent, resilient and liquid.

ICAP's role in the market is as an execution intermediary, and it is from that perspective that we offer our comments. Our BrokerTec division operates what we believe to be the world's leading fully electronic anonymous U.S. Treasury security ("UST") trading platform utilized by dealers, banks, and non-bank professional trading organizations. Our Global Broking division offers voice and hybrid voice-electronic execution of Treasury bills and off-the-run UST for a similar customer base. Over the past year, trading on BrokerTec has averaged about 15,000 transactions per day and $160 billion in average daily notional

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[1] ICAP is a leading markets operator and provider of post trade risk mitigation and information services. The Group matches buyers and sellers in the wholesale markets in interest rates, credit, commodities, FX, emerging markets and equity derivatives through voice and electronic networks. Through its post trade risk mitigation and information services ICAP helps customers manage and mitigate risks in their portfolios. For more information, go to www.icap.com.

[2] *Notice Seeking Public Comment on the Evolution of the Treasury Market Structure*, 81 Fed. Reg. 3927 (Jan. 22, 2016).

trading volume. While precise numbers are unavailable, we believe our Americas Broking business accounts for a meaningful percentage of interdealer trading in the off-the-run market.

General Comments

While we have responded to certain specific RFI questions below, we want to initially suggest some general considerations about the market that we believe should be taken into account in any contemplated policy response.

Diffuse Regulation – any policy response needs to recognize that any envisioned solution will need to cut across multiple regulatory regimes and structures. For example, many broker-dealers in the UST market are registered with and regulated by the SEC and FINRA. Banking entities, however, are also permitted to engage in UST broking and dealing activity, and would be regulated instead by the relevant banking supervisor rather than the SEC and FINRA. Further, beyond the cash market, market participants managing their interest rate exposure will actively trade not just the cash market but the futures and swaps markets as well. Those markets are regulated by the CFTC, the NFA, and exchanges and swap execution facilities acting in an SRO capacity. While the differing forms of regulation certainly do not preclude making enhancements to the market, it is critical that policymakers ensure their proposals adequately capture this state-of-affairs, both to ensure effective implementation and to foreclose unwanted changes to market participant behavior to take advantage of perceived regulatory arbitrage opportunities.

Trading Venue Market Structure – the UST trading market has evolved largely in response to market participant needs rather than being shaped by regulatory mandates. It is an over-the-counter market, where participants can execute transactions by voice, on electronic platforms oriented towards a dealer-to-customer request-for-quote model, and on electronic platforms like BrokerTec that are oriented towards a professional trader order book model. Unlike the equity markets, there is no concept of a national best bid or offer against which to measure executions, and unlike futures, there is no requirement that all transactions be exchange-traded and centrally cleared.

As policymakers consider any changes to market structure, we would urge that any such changes be undertaken cautiously, based on rigorous analysis and a clear sense of the desired goals. Experience shows that the different models have both strengths and weaknesses.

The U.S. futures model, where the exchanges have a vertical monopoly based on their control of clearing houses, brings all trading interest to a single venue and manages the leverage associated with the product through required clearing. The model may be less successful, however, in bringing about lower prices and customer-friendly innovations due to the absence of meaningful competition.

Conversely, the equity markets are characterized by multiple execution venues, a Reg NMS requirement to execute at or within the publicly disseminated national best bid and offer available on any venue, and the management of leverage through margin rules administered at the broker-dealer customer account level. While this model has contributed to competitive innovation and pricing, it has also raised concerns about whether the disparate execution venues create opportunities for undesirable behavior across venues and inadequately managed risk linkages.

For these reasons, we believe there is considerable uncertainty as to what in fact is the most preferred trading venue structure, even as one readily agrees any such structure should be measured by its fairness, transparency, resiliency, and facilitation of liquidity. That uncertainty counsels caution, particularly in a marketplace for an instrument that is so central to the functioning of U.S. and world markets.

Instrument Categories – the UST market can usefully be thought of as divided into two categories, on-the-run and off-the-run instruments, and the distinctions between the two should be reflected in policy choices. On-the-run instruments consist of the most recently issued 2-year, 3-year, 5-year, 7-year, 10-year, and 30-year bonds, and those instruments are highly liquid upon issuance and serve as critical benchmarks and pricing references across the financial markets. Off-the-run instruments consist of all seasoned UST products, and they are far less liquid and far less significant to the pricing of other instruments. Each category currently trades quite differently, and given their different liquidity characteristics and importance to the market, one regulatory approach is unlikely to be suitable for both categories of instruments.

October 15, 2014 – the volatility of October 15, 2014 certainly merits the review that policymakers have undertaken, but it's also important to remember that in many respects the market functioned very well that day. In the case of BrokerTec, we saw record trading activity of $456 billion and that activity was processed, cleared, and settled without incident. Notwithstanding the volatility, there were transactions at price points up and down the curve. We do not believe that event alone should be a basis for material changes to the market that are not demonstrated by study and analysis to be clear improvements.

Comments on RFI

ICAP's response to specific parts of the RFI are set forth below. We have responded to those requests where we believe our perspective as a trading venue operator may be most useful.[3]

Section I. Further Study of the Evolution of the U.S. Treasury Market and the Implications for Market Structure and Liquidity.

Question 1.5. What changes to the U.S. Treasury market structure, whether through public or private sector initiatives, might be advisable given the recent and expected future evolution? What role should the public sector play in driving or facilitating these changes?

Answer: We believe that the US Treasury Market largely functions quite well in its current iteration. As we discuss below, certain changes, such as increased reporting to the official sector and setting minimum operational and risk management requirements for all UST trading platforms and venues, are sensible and by their nature will need to be driven by public sector mandates. For other changes that have been discussed we would urge careful consideration before imposing new requirements in areas such as mandated clearing, intra-day margining, limitation of high-frequency strategies, or cross-market trading halts. These are all worth careful study but we do not believe that the perceived benefits of mandates in these areas have yet been demonstrated to outweigh the perceived costs.

Question 1.6. **What are the benefits and risks from the increased speed with which secondary market transactions take place? Do these benefits and risks differ across individual products (e.g., on-the-run versus off-the run securities?) How have market participants and trading venues**

[3] Our comments are keyed to the provisions as enumerated in the RFI for ease of reference.

responded to, or facilitated, improvements in speed, and how, if at all should policy makers respond?

Answer: We do not believe the official sector should regulate transaction speed. High-frequency strategies, which are employed by many different market participants, add additional liquidity provision to the ecology of the market and help narrow bid-offer spreads. High-frequency traders can certainly act on prices faster than slower traders, but it is not clear that such advantages are unfair (and there will always be market participants for whom speed is more important than for other market participants).

We do believe, however, that it is critical for regulators and regulated firms to police and prevent behaviors such as spoofing, layering, and improper self-trading that may be more easily facilitated with high-frequency strategies. We also believe that trading venues should clearly disclose their material operating policies and procedures so that market participants understand how trading on that venue occurs and can make an informed choice about what type(s) of venue(s) they want to utilize.

We appreciate the concerns that have been raised about the diminishing returns of an "arms race" for greater and greater speed, as well as concerns about whether the liquidity provided by high-frequency trading may have meaningfully different attributes than other types of liquidity. However, we do not see an easy or obvious regulatory response to these issues.[4] ICAP believes that permitting trading venues to innovate, and requiring them to provide transparency to their participants, is more likely than official sector mandates to lead to a marketplace that serves the differing needs of different market participants.

Section II. Continued Monitoring of Trading and Risk Management Practices Across the U.S. Treasury Market and A Review of the Current Regulatory Requirements Applicable to the Government Securities Market and Its Participants.

Question 2.1(b). To what extent should venue-level risk management practices be uniform across Treasury cash and futures venues? For example, should there be trading halts in the Treasury cash market and should they be coordinated between Treasury cash and futures markets, and if so, how?

Answer: We believe that UST trading venues and futures venues should maintain robust venue-level risk management, and that it is appropriate for the official sector to set minimum risk management standards (as, for example, the SEC has done with the promulgation of Rule 15c3-5 for those providing market access). We also support the adoption of best practices and voluntary standards like those promulgated by the Treasury Market Practices Group.

We do not at this time support mandatory trading halts either within the cash market alone or coordinated with the futures markets. As an initial matter, investors expect to be able to transact during market hours, and anything that contravenes that expectation should be presumptively disfavored. That is even more so for on-the-run UST instruments, which serve as critical benchmarks across the financial markets. Indeed, a trading halt in UST would effectively disrupt trading in all other instruments that trade on a spread to

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[4] The notice and comment process that is currently taking place at the SEC over the application for the IEX equities exchange is illustrative. IEX proposes to utilize a speed bump to minimize the advantages of a high-frequency strategy, yet knowledgeable and passionate market participants are deeply divided over whether the IEX model is more or less fair than existing models. See, e.g., "Plan for New Stock Exchange Stirs Furious Debate," *New York Times*, November 16, 2015.

the benchmark, such as interest-rate swaps, off-the-run treasuries, agency and MBS securities, and investment-grade corporate bonds. Second, we believe the efficacy of trading halts in other markets is decidedly unsettled – for example, implementation of a trading halt during the stock market declines in China earlier this year appeared may have exacerbated volatility rather than mitigated it.[5] Third, we question the ability to enforce a trading halt in the UST market, given that it is an over-the-counter market with no exchange trading requirement. Even if certain venues halted trading, market participants could still transact through other venues or on the telephone.

Question 2.6. Many of the standards applicable to the U.S. securities, commodities and derivatives markets are not applicable to the US Treasury cash market. Which differences, if any, should be addressed and how should standards be aligned?

Answer: We do not believe that the UST trading structure needs to be aligned to the commodities and derivatives markets. As noted in our general comments, existing market structure models have their strengths and weaknesses, and we do not believe there is a basis to conclude that the futures or derivatives models are superior to a structure that has worked well for UST's for an extended period.

However, we do believe that the official sector should increase the standards applicable to UST trading venues. Currently such venues are exempt from registration as Alternative Trading Systems under Reg ATS if their products include only U.S. government securities. We believe this exemption should be removed.

We also believe that the requirements for a UST ATS should be enhanced, and more tailored to the attributes of the UST market.[6] A UST ATS should be subject to the requirements of SEC Rule 15c3-5, which requires platforms to implement important risk-mitigation tools when providing market access.[7] We also believe a UST ATS should be required to meet defined standards in areas such as business continuity, resiliency, technology change control, the reporting of system problems and issues to the official sector, and frequency of audits.

Question 2.7. Should self-trading be expressly prohibited in the cash Treasuries market? Does self-trading provide any benefits to the markets? Are there risk management tools, either at trading firms or at trading platforms, which can effectively reduce levels of self-trading and improve trading efficiencies?

Answer: Self-trading can provide benefits to the markets. To the extent a market better reflects "true" value the more it reflects the available sentiments about prices, independent sentiments even from within the same organization may contribute usefully to price discovery. In addition, many large organizations operate multiple businesses that may participate in the UST market, and if those businesses are operating independently, going outside the firm to execute and unintentionally matching with an independent part of the same organization can help that organization validate the accuracy of pricing.

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[5] See, e.g., "China Suspends Stock Circuit Breaker Days After Introduction," *Bloomberg*, January 7, 2016.

[6] Reg ATS was issued originally to address the proliferation of internet based equity trading platforms, and many of its provisions are focused on obligations associated with market share levels in equity stocks.

[7] We believe that by its terms Rule 15c3-5 may already apply to even an ATS that is not required to register as such, but we believe explicit clarification of that point would be helpful to the marketplace.

For those reasons, we believe a prohibition on self-trading is unwarranted. However, we recognize the potential for improper self-trading to be harmful to markets and believe the public sector should subject such activity to regulation and provide needed guidance.

We believe the approach that FINRA has taken in this area is sensible. FINRA Rule 5210 has made it clear that "self-trading" between different parts of the same legal entity is not inherently improper[8] provided it reflects truly independent activity. However, FINRA specifies that firms that may engage in self-trading need to affirmatively monitor their activity, ensure it is truly independent, and consider whether high volumes of even independent self-matching should continue. The FINRA Rule, however, applies by its terms only to FINRA members, generally registered broker-dealers. Policymakers should consider regulations that would apply these requirements to other market participants as well.

We also believe that trading venues should have in place policies and procedures reasonably designed to detect, prevent and report suspicious activity, including activity that may constitute improper self-trading. Platforms should also develop and make available to market participants tools that enable them to manage their potential to self-trade on the platform, for example by permitting them to block their capacity to self-match in identified circumstances. Platforms should also conduct routine monitoring of trading activity, and include in customer agreements an obligation to conduct activity in compliance with all laws and regulations, and a right for the platform to terminate access in the event of problematic activity. In this regard, we think the marketplace would benefit from more detailed official sector guidance on best practices for monitoring potentially problematic self-trading behavior.

Section III. Assessment of the Data Available to the Official Sector on US Treasury Cash Securities Market.

Questions 3.2. What frequency and type of additional data reporting to the official sector is necessary for it to effectively monitor functioning of the US Treasury markets, including cash, futures and financing markets? What level of granularity is necessary for sufficient monitoring to be performed (e.g., transaction data, inventories or positions, order book data, and other additional data) across venues?

- **(a) Should all transactions in securities issued by the Treasury be subject to reporting or should reporting be limited to secondary market transactions or some other subset?**
- **(b) Should repurchase agreement transactions be reportable?**

Answer: We support the reporting to the official sector of all UST transactions, including repurchase agreements, as well as interest-rate futures and interest-rate swaps. These instruments all play a role in the transfer of interest-rate risk and bear on the development and integrity of benchmark prices. The official sector should have available to it, and be able to share within and across the sector as needed, all information needed to perform its oversight role effectively.

With respect to data reporting details and specifications, we believe it is difficult to do justice to that complex subject within the confines of a Comment Letter, and we would advise that a task force containing representatives from a cross-section of market participants be convened to make

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[8] See FINRA Rule 5210 supplementary materials .02.
http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=8726

recommendations to the official sector. On a conceptual level, though, we think a data reporting regime should incorporate the following:

- Specification of data to be provided in real time versus data that can be provided on a batch basis or even only upon request. For example, real-time data for on-the-run securities could include at a minimum last trade information (price, volume, time of execution), top of the order book, legal entity identifier, and trader identifier.
- Application to all significant trading intermediaries. As the UST market is an over-the-counter market, the reporting regime must ensure that it applies to any intermediary (including bank intermediaries) that can execute transactions, not just those that are registered as an ATS or that are actively marketed as trading venues. This is both to ensure comprehensive coverage of trading activity, and to ensure that trading does not migrate to less transparent venues.
- Consistent data specifications across the official sector. A common approach across the different public sector agencies and regulators should incorporate standard legal entity, trader, and instrument identifiers, as well as a commonly agreed format for reporting data fields. Reporting parties should be able to report to one central recipient, rather than to multiple official sector points.
- Address internalization of flow. A good deal of trading activity occurs internally within large dealer and banking organizations, and that activity can have significant informational value. We believe the official sector should consider ways to capture that activity to better understand its relationship to benchmark pricing.

Section IV. An Assessment of the Data Available to the Public on U.S. Treasury Cash Securities Markets

Question 4.1. Is the publicly available information for the U.S. Treasury market trading activity [9]sufficiently transparent to foster an efficient, healthy, and liquid market?

Answer: Yes. We believe the market is highly transparent, efficient and liquid and do not support the imposition at this time of increased public reporting of UST transactions. First, we and many others already make extensive real-time trading data and analytics commercially available directly to customers and via third-party market data vendors such as Bloomberg and Thompson Reuters. Second, we believe the UST market is primarily an institutional market, not a retail market, and institutional parties have ample pricing data available, not just from the foregoing commercial sources, but from dealer counterparties as well. Third, UST prices are very transparent and quoted constantly on TV (MSNBC), on Bloomberg, by market commentators, and in business sections of US newspapers, and in other places as well. Fourth, any trade reporting regime entails initial and ongoing operational costs for market participants, which given the large number of OTC intermediaries, many of them small, could be quite significant – such costs should only be imposed upon a showing that they are outweighed by the commensurate benefits.

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[9] A FINRA-type reporting regime has been discussed as a possible policy initiative in this area. We would note that current TRACE parameters, which provide for a 15-minute reporting window and a 15-minute dissemination delay, are ill-suited to the on-the-run market, where the six main cusips are highly liquid and prices often change by the millisecond.

Conclusion

We appreciate the opportunity to comment on the RFI. The UST market continues to be the deepest and most liquid market in the world, and we are committed to working constructively with the official sector and market participants to see that it stays that way.

If we can be of further assistance, please don't hesitate to contact us at dan.cleaves@btec.com (212) 521-4707, or Jerald.Irving@us.icap.com at 212-815-9544.

Regards,

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