September 14, 2026

***Via Electronic Submission***

Christopher Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, D.C. 20581

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549

**Re: Joint Request for Comment on Further Definition of "Swap" and "Security-Based Swap" and on Alternative Compliance (CFTC RIN 3038-AF71; SEC Rel. No. 33-11424; No. 34-105735; File No. S7-2026-21; RIN 3235-AN79)**

Dear Mr. Kirkpatrick and Ms. Countryman:

MFA[1] submits these comments to the Securities and Exchange Commission ("**SEC**") and the Commodity Futures Trading Commission ("**CFTC**" or, together with the SEC, "**Commissions**") in response to the Commissions' Joint Request for Comment on Further Definition of "Swap" and "Security-Based Swap" and on Alternative Compliance ("**Joint RFC**").[2]

MFA and its members appreciate this opportunity to comment on the important questions raised by the Joint RFC. The issues addressed span a broad spectrum—from

[1] Managed Funds Association (MFA), based in Washington, D.C., New York City, Brussels, and London, represents the global alternative asset management industry. MFA's mission is to advance the ability of alternative asset managers to raise capital, invest it, and generate returns for their beneficiaries. MFA advocates on behalf of its membership and convenes stakeholders to address global regulatory, operational, and business issues. MFA has more than 180 fund manager members, including traditional hedge funds, private credit funds, and hybrid funds, that employ a diverse set of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors diversify their investments, manage risk, and generate attractive returns throughout the economic cycle.

[2] Joint Request for Comment on Further Definition of "Swap" and "Security-Based Swap" and on Alternative Compliance, 91 Fed. Reg. 37873 (June 24, 2026) ("**Joint RFC**"), available at: https://www.govinfo.gov/content/pkg/FR-2026-06-24/pdf/2026-12743.pdf.

the regulatory treatment of novel and rapidly evolving product categories to questions affecting well-established markets in which our members have transacted for decades. Given the breadth of the Joint RFC and the nascent state of both the markets and the regulatory framework developing around novel products such as event contracts and perpetual contracts, we offer a set of principles that we hope the Commissions will consider as they develop that framework.

In particular, we believe the Commissions should ensure that the regulatory framework for such novel products provides robust protections for the securities markets and those who participate in them and use the securities markets to raise capital. With respect to more established markets, where our members have extensive, direct experience with the practical consequences of the current regulatory framework and have made significant investment in systems and policies to shoulder the burdens imposed on them by the compliance framework that applies to swaps, our requests are narrowly aimed at removing unwarranted compliance burdens; beyond those, we urge the Commissions not to adopt changes that would add to the burdens already borne by MFA members.

## I. Executive Summary

Institutional investors—including public and private funds and the professional investment advisers that manage capital on their behalf—contribute meaningfully to well-functioning markets by allocating capital efficiently, enhancing liquidity, deepening price discovery, and bringing specialized expertise and disciplined risk management. Their participation also promotes portfolio diversification and broad public access to investment opportunities. Should novel products such as event contracts and perpetual contracts reach meaningful scale, responsible institutional participation would likely deliver these same benefits, along with heightened demand for robust governance, transparency, and surveillance.

We therefore encourage the Commissions to develop a framework that both facilitates responsible institutional participation and safeguards investor protection and market integrity. To that end, we respectfully offer the following recommendations:

- The Commissions should ensure the regulatory framework that develops around novel products provides the necessary protections to the securities markets and market participants.

- The Commissions should revise their prior interpretation of cross-currency ("**compo**") equity swaps, consistent with the underlying economics of such transactions.

- The Commissions should require the affirmative approval of both Commissions, in place of self-certification, before a novel product that implicates each agency's regulatory interest is listed for trading.

## II. Discussion

### A. The Commissions should ensure the regulatory framework that develops around novel products provides the necessary protections to the securities markets and their participants

We welcome innovation in the financial markets and appreciate the Commissions' continued commitment to providing a regulatory framework that both encourages innovation and safeguards market integrity. The emergence of novel product categories such as event contracts and perpetual contracts[3] raises important questions about the appropriate regulatory characterization for such products and the regulatory obligations that should be in place to enable their trading.

The Commissions should develop a regulatory framework for novel products that protects the securities and derivatives markets and market participants. As part of this process, the Commissions should ensure that each Commission that has a regulatory interest in a novel product has the appropriate opportunity to review such product, prior to it being listed for trading on a regulated marketplace. As we discuss below, it is not always clear when a product implicates the regulatory interest of each agency, so the Commissions should propose a framework setting out the relevant factors. In particular, both Commissions should be required to approve a novel product before it is listed where the product implicates each agency's regulatory interest, in place of the current approach that permits market participants to self-certify.

As an overarching principle, MFA members submit that the SEC serves as the principal guardian of investor protection in the U.S. securities markets, a mandate reinforced by a comprehensive and time-tested ecosystem of safeguards.[4] Chief among those safeguards is the SEC's comprehensive market surveillance system, which the SEC has built out over decades to detect, deter, and pursue insider trading, the misuse of material non-public information, and other forms of manipulation in the securities markets. Guarding against insider trading and preserving investor protection and confidence in the integrity of the securities markets is a principal reason we urge that securities-related products be regulated by the SEC rather than the CFTC.

Accordingly, to the extent that a novel product implicates the securities markets, the SEC should be the relevant regulatory agency for such products. For the same reasons, the Commissions should approach the concept of Alternative Compliance with caution and ensure that Alternative Compliance is not used as a mechanism to change the overarching oversight framework and allocation of regulatory jurisdiction over the

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3 While many of the same concerns discussed herein are relevant to exchange-traded funds ("**ETFs**") consisting of such novel products, we do not directly address concerns related to ETFs in this letter. We note in this regard that the SEC has released a separate request for comments related to novel ETFs. *See* SEC, Request for Comment on Novel ETFs, 91 Fed. Reg. 40647 (July 2, 2026), available at: https://www.govinfo.gov/content/pkg/FR-2026-07-02/pdf/2026-13423.pdf.

4 *See, e.g.*, FINRA Rule 2111 (Suitability); Regulation Best Interest, 17 C.F.R. § 240.15l-1; Options Disclosure Document, available at: https://www.theocc.com/company-information/documents-and-archives/options-disclosure-document, 17 C.F.R. § 240.9b-1.

securities and commodities markets established by Congress. While permitting compliance with one Commission's requirements to satisfy substantially similar requirements of the other may be appropriate for certain operational or reporting obligations, MFA encourages the Commissions to consider carefully whether Alternative Compliance is appropriate where it would allow a product that affects the securities markets to be outside of the securities regulatory perimeter for key regulatory functions such as surveillance. [5]

MFA generally favors clear regulatory responsibility and ensuring that such regulatory responsibility supports market integrity. As such, where a product implicates the securities markets, the Commissions should ensure that the SEC, the regulator charged with protecting those markets, retains a complete view of trading activity necessary to conduct effective surveillance and authority to enforce the securities laws. The Commissions should not adopt an Alternative Compliance framework that undermines the SEC's ability to do that. This principle cuts both ways: just as products that are fundamentally commodity in nature are best surveilled by the CFTC, products that Congress placed within the securities regulatory perimeter—and as to which the SEC alone possesses the requisite enforcement authority over insider trading and manipulation—are best surveilled by the SEC. The objective is not to diminish either Commission's role, but to ensure that surveillance responsibility follows regulatory expertise and statutory authority so that no gap emerges between them. Similarly, we would be concerned if surveillance responsibilities are divided in a manner that leaves no regulator with sufficient visibility, authority, and expertise to detect and prevent cross-market manipulation. The SEC has already built out a comprehensive surveillance system for insider trading and market manipulation and should apply the same level of rigor to preventing abuse and manipulation in markets for novel products. Bifurcating trading of related products along regulatory lines and bifurcating oversight risk creating precisely the gaps in oversight that undermine investor protection and confidence. It could also

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5 One appropriate use of Alternative Compliance would be to address a product referencing a security index that migrates between broad-based and narrow-based status—and potentially back—as a result of temporary changes in index composition, a shift that can move the product between the "swap" and "security-based swap" regimes. *See* 7 U.S.C. § 1a(35); 15 U.S.C. § 78c(a)(55) (defining "narrow-based security index"). The Commissions have adopted tolerance and transition mechanisms to soften these transitions. For example, the Commissions have addressed (i) the 45-business-day tolerance and subsequent three-month transition periods applicable to security futures on indexes that cross between broad- and narrow-based status (*see* 17 C.F.R. §§ 41.11–41.14; 17 C.F.R. §§ 240.3a55-1 to 240.3a55-4; Method for Determining Market Capitalization and Dollar Value of Average Daily Trading Volume; Application of the Definition of Narrow-Based Security Index, 66 Fed. Reg. 44490 (Aug. 24, 2001)), and (ii) the analogous tolerance periods (likewise measured as no more than 45 business days over three consecutive calendar months) for swaps and security-based swaps referencing such indexes (*see* 17 C.F.R. § 240.3a68-3). While helpful, these provisions can still require market participants to shift a product between regulatory regimes based on transient fluctuations in an index. Permitting such a product to remain subject to a single, consistent set of requirements during these periods would reduce unnecessary operational disruption and compliance cost.

invite regulatory arbitrage, allowing market participants to elect the less protective regime.

To the extent that the CFTC also has a regulatory interest in such products, it should coordinate with the SEC. The mechanisms needed to achieve this coordination are already available. The Commissions have recently strengthened their cooperation—including through a memorandum of understanding and a joint harmonization initiative that provide for regular consultation, data sharing, advance notification, and coordinated oversight—and those mechanisms furnish a ready foundation for the Commissions to close regulatory gaps. However, such cooperation and the operational efficiencies gained from Alternative Compliance should never have the effect of depriving the SEC of a complete view of the trading activity in the securities and related markets.

The Commissions also should generally ensure that the regulatory framework governing a particular novel product adequately addresses the risk of regulatory arbitrage and affords appropriate investor protections that are tailored to the characteristics and risks of the product. A framework built on these principles would do more than guard against abuse; it would create the conditions under which responsible institutional participation can develop. Just as institutional investors bring liquidity, price discovery, and disciplined risk management to established markets, their participation in novel product markets would deliver those same benefits—but only where robust governance, transparency, and comprehensive surveillance give them the confidence to participate at scale.

### 1. Event Contracts

Event contracts raise complex characterization questions. MFA believes the Commissions should answer such questions with objective, ex ante criteria that can be applied at listing. For example, an event contract that "directly affects the financial statements, financial condition, or financial obligations of [an] issuer" would be a security-based swap under the statutory definition.[6] However, as the Joint RFC suggests, what it means for an event contract to "directly affect[] the financial statements, financial condition, or financial obligations of [an] issuer" would benefit from further clarity in the event contracts context,[7] as there are certain events that may have tenuous impact on the financial condition of an issuer and where it is unclear if such event meets the statutory definition of a security-based swap.

One of our principal concerns is that novel products could be brought to market under a regulatory framework that undermines the integrity of the securities markets. There are several relevant risks that the Commissions should consider.

First, an event contract whose settlement is related to company-specific information—such as a contract settling on a corporate event including a merger, acquisition, earnings announcement, or initial public offering—raises issues regarding price formation, capital formation, and market integrity in the securities markets. For

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6 *See* 15 U.S.C. § 78c(a)(68)(A)(ii)(III).

7 *See* Joint RFC, Question 7.

example, such contracts could permit price discovery related to securities to occur outside of the regulatory framework of the federal securities laws, which can fragment liquidity and weaken the pricing signals on which investors and issuers rely when they raise capital.

In addition, such products give rise to the risk of market manipulation, which would arise if the regulatory framework for such products does not provide for comprehensive surveillance of trading activity across such products and related securities markets. For example, trading in an event contract linked to a specific company could be a proxy for trading in the securities of such company. Without appropriate surveillance and protections against market manipulation (including on a cross-market basis), traders could exploit or misuse material non-public information about the company or engage in other manipulative trading activity. Put differently, absent comprehensive and consolidated surveillance, event contracts could become a venue for insider trading and other abuses that the federal securities laws are designed to prevent—conduct that erodes investor confidence in the fairness and integrity of the securities markets. The SEC has spent decades building the surveillance capacity needed to detect precisely this conduct, and that capacity is best preserved by assigning oversight of securities-related event contracts to the SEC rather than bifurcating it across agencies or asking the CFTC to replicate it. Where oversight is divided between regulators, there is a risk that no single regulator has sufficient visibility across both the event-contract market and the related securities market to identify and act on manipulative trading activity.

Indeed, the insider-trading risk that event contracts present is in certain respects more acute than in the securities markets themselves. Where an event contract settles directly on a corporate outcome—such as an earnings result, a merger, or a regulatory approval—a person in possession of material non-public information about that outcome can monetize the information directly and with near certainty, whereas in the equity markets the same information ordinarily bears on price only indirectly and imperfectly. That more direct payoff structure both heightens the incentive to misuse confidential information and complicates its detection absent purpose-built, cross-market surveillance. These concerns are not hypothetical: enforcement authorities have already pursued charges arising from trading on confidential corporate information in event-contract and prediction markets, and have signaled that the misuse of material non-public information will be policed in these markets as rigorously as in any other. Assigning surveillance of securities-related event contracts to the regulator that has spent decades developing the tools to detect trading ahead of market-moving corporate events is therefore essential to preserving investor confidence.

The Commissions also should consider the effects that substantial migration of economically similar activity from the securities markets into event contract markets could have on the functioning of those markets. The U.S. securities markets currently provide deep liquidity, efficient price discovery, robust transparency, and support for capital formation. To the extent that novel products facilitate trading activity that functions as a substitute for trading in securities or security-linked instruments, the Commissions should consider whether such activity could fragment liquidity, weaken price formation in the securities markets, or diminish the effectiveness of existing market structures and investor protections. These concerns are especially acute where activity migrates to products that are subject to a different regulatory framework or surveillance regime, potentially creating gaps in oversight and opportunities for regulatory arbitrage. Any framework governing novel products should therefore seek to preserve the integrity and efficiency of the existing securities markets while accommodating responsible innovation.

We urge the Commissions to structure surveillance so that, for any set of related products, a single regulator holds a complete view of trading activity across those products—assigned according to the nature of the products and the markets they most directly affect, with robust coordination where jurisdictional interests overlap. Consolidating surveillance responsibility within a single agency enhances the ability to detect abusive or manipulative conduct across related markets, although the Commissions should coordinate where statutory jurisdiction overlaps. For products related to securities, this should be the SEC and include jurisdiction with respect to securities and products that may influence, affect, or otherwise be used to manipulate the securities markets. The SEC has already developed the surveillance infrastructure necessary to police insider trading and manipulation in the securities markets, and there is no reason to bifurcate that function or to require the CFTC to duplicate that infrastructure at significant and unnecessary cost. Consolidating surveillance of securities-related products in the SEC avoids that duplication of resources while best protecting investors and preserving their confidence in the integrity of the markets. We recognize that questions of regulatory characterization and jurisdictional allocation are complex and may not always yield a single clear answer.

However, the Commissions should not allow that complexity to result in a fragmented surveillance framework in which no single regulator has a complete picture of trading activity that affects the securities markets. Robust surveillance infrastructure benefits all market participants, including the institutional investors whose participation strengthens these markets. Institutional participants typically demand—and their presence tends to promote—robust governance, transparency, comprehensive surveillance, and sound operational controls. A regulatory framework that consolidates surveillance responsibility and provides a complete view of trading across related products supports these expectations and enhances the ability to detect and deter manipulative conduct across markets, and it does so while fully preserving each Commission's authority over the products within its respective domain and the coordination mechanisms the Commissions have recently established.

In addition, the Commissions should develop a framework that requires the affirmative approval of both Commissions before a novel product is brought to market that implicates the regulatory interests of each Commission. A process by which both Commissions have the opportunity to assess the proper characterization and therefore the market integrity, investor protection, and surveillance implications of a new product before it reaches the market, would alleviate this concern. This process should replace the current approach, which relies on market participants self-certifying prior to registration.

In principle, the MFA recommends that the Commissions maximize regulatory clarity by clearly segregating and assigning financial instruments to a single regulator wherever possible and reducing the scope of overlapping jurisdiction wherever possible. The Commissions should not, without serious consideration, expand the products over which jurisdiction is shared. MFA is concerned that this may lead to regulatory arbitrage in that market participants could select a less onerous, less protective regime to apply to a product than the one developed by the primary regulator.

### 2. Perpetual Contracts

#### *I. Background and Key Structural Features*

Perpetual contracts are a novel product category that first gained traction in offshore digital asset markets, but that have recently become accessible to U.S. participants following the CFTC's approval of certain digital commodity perpetual contracts as futures contracts.[8] While perpetual contracts on non-digital-commodity underliers remain confined to non-U.S. venues for now, trading venues in the U.S. are actively pursuing offering such products across a wider range of asset classes, making it imperative that the Commissions establish a clear regulatory framework for such products.

Perpetual contracts have unique characteristics that the Commissions should take into consideration when determining the appropriate safeguards that must be in place before such contracts are made available. Perpetual contracts offer leveraged exposure to a particular reference underlier, and allow market participants to take either the long or short side of the contract.[9] Perpetual contracts have a pricing mechanism that differs from that used in connection with traditional futures contracts. Instead of having a fixed settlement date like traditional futures contracts, perpetual contracts use a funding rate mechanism to incentivize convergence between the underlying spot price and the perpetual contract price.[10] In addition, because there is no fixed settlement date, there are no successive settlement dates for perpetual contracts and consequently no "forward curve" (i.e., the curve with respect to traditional futures contracts that projects future prices of the same underlying asset at different specified times).

The perpetual contracts that are currently available to U.S. participants are traded on a 24/7 basis. CFTC staff have issued guidance recognizing that, while continuous trading may be appropriate for digitally native asset classes, other markets (with more concentrated participant bases, regional trading patterns, and specialized hedging needs) may not be suited to 24/7 operations.[11]

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8 *See* Policy Statement Concerning the Listing of Perpetual Contracts, 91 Fed. Reg. 33160 (June 3, 2026); Order Approving KalshiEX LLC BTCPERP Futures Contract (May 29, 2026), available at: https://www.govinfo.gov/content/pkg/FR-2026-06-03/pdf/2026-11020.pdf.

9 *See* Order Approving KalshiEX LLC BTCPERP Futures Contract, at 7 (May 29, 2026), available at: https://www.cftc.gov/filings/documents/2026/orgdcmkexbtxperporder26601.pdf.

10 *Id.*

11 *See* CFTC Letter No. 26-16, Staff Advisory for Extending Trading and/or Clearing Operations to a 24 hours-a-day, 7 days-a-week Basis (May 29, 2026).

MFA and our members share the CFTC's view that perpetual contracts on asset classes beyond digital commodities present unique considerations warranting their own separate, careful analysis.[12] We likewise support the CFTC's position that parties seeking to offer perpetual contracts should do so through an affirmative approval process rather than offer such products solely by way of self-certification.[13] MFA urges the Commissions to formalize this approach by establishing a concrete, codified approval framework, and we respectfully submit the observations below to assist the Commissions in crafting an appropriately tailored regulatory regime for perpetual contracts. The safeguards we describe below are not obstacles to the development of these markets but preconditions for their responsible growth. Institutional investors of the kind MFA represents are most likely to participate—and to bring their liquidity and risk-management discipline to bear—where pricing integrity, sound risk controls, and coordinated surveillance are assured.

## *II. Key Considerations the Commissions Should Take into Account in Developing a Regulatory Framework Governing Perpetual Contracts*

The Commissions should articulate with greater specificity the requirements that must be satisfied before perpetual contracts referencing non-digital-commodity underliers may be offered for trading. At a minimum, the Commissions should ensure the framework achieves the following:

- **Integrity of the Spot Price and Funding Rate**. The Commissions should ensure that the spot market for the proposed underlier is sufficiently liquid and reliable, and that the funding rate mechanism will function effectively given the characteristics of that market. The Commissions should also ensure that the omission of traditional cost-of-carry inputs (such as storage, transportation, and financing) does not introduce pricing anomalies that would not arise in the context of a conventional futures market. Prior to approving a proposed commodity perpetual contract, the Commissions should rigorously examine the reference price methodology of such contract.

- **Hedging**. An open-ended contract without a settlement date does not generally replicate the term-structured hedging that traditional futures provide. The Commissions should ensure that perpetual contracts do not undermine the hedging or risk-mitigation functions served by traditional futures.

- **Manipulation Risk and Regulatory Arbitrage**. The Commissions should ensure that perpetual contract markets are not susceptible to manipulation and that the applicable regulatory framework does not permit regulatory arbitrage.

- **Risk Management for Extended and Continuous Trading**. To the extent a proposed perpetual contract would trade beyond standard market hours, the

[12] *See* Request for Comment on the Extension of Standard Futures Contracts to 24/7 Trading and on Perpetual Contracts Referencing Physically Delivered or Storable Energy Commodities, 91 Fed. Reg. 38334 (Jun. 25, 2026).

[13] *See* Policy Statement Concerning the Listing of Perpetual Contracts, 91 Fed. Reg. 33160, 33161-2 (June 3, 2026).

Commissions should ensure that positions can be adequately managed in the absence of corresponding around-the-clock collateral movement, that auto-liquidation or margin call mechanisms are appropriately employed, and that such mechanisms are suitable for the particular underlier.

- **Risk Mutualization**. The Commissions should take into account loss mutualization for cleared contracts at both the clearing house and the clearing member level when determining the appropriate risk management framework for perpetual contracts.

- **Liquidity Displacement and Price Formation**. The Commissions should ensure that the introduction of a perpetual contract market does not divert trading volume away from the markets for the underlying assets, and does not impair the capital-raising function of the equity markets or the efficient operation of physical commodity markets.[14]

*III.* *The Commissions Should Carefully Consider the Appropriate Regulatory Treatment for Perpetual Contracts*

The Joint RFC asks whether "there [is] a need for greater clarity regarding whether a cash-settled "perpetual" contract referencing an equity security could be treated as a security future."[15] Given that the existing joint-regulatory framework for security futures (established by the Commodity Futures Modernization Act of 2000[16]) was not developed by Congress with perpetual contracts in mind, MFA urges the Commissions to evaluate whether the security futures framework provides the safeguards necessary to accommodate perpetual contracts on equity underliers (or whether the security futures framework could be adapted to provide such safeguards).

The Commissions also should consider whether a framework involving sole SEC oversight would be more appropriate for purposes of regulating perpetual contracts that reference equity securities. In conducting that evaluation, the Commissions should focus on the economic and functional characteristics of a perpetual contract—including its standardized terms, fungibility, capacity to be closed out through an offsetting position, and price-convergence mechanism—rather than on the nature of the underlying asset alone, so that instruments receive regulatory treatment appropriate for the characteristics of the particular instrument and the risks they pose to customers and opportunities for regulatory arbitrage are minimized. At the same time, we caution that the security futures framework has been largely dormant commercially for many years

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14 In addition, if novel products were to become a significant alternative to traditional securities or derivatives markets, the Commissions should consider the potential for reduced transparency, conflicting pricing signals across markets, diminished hedging effectiveness, and increased complexity and concentration arising from parallel market structures. These risks warrant careful consideration before products that implicate the securities markets are permitted to develop outside a framework that provides comprehensive and coordinated oversight.

15 *See* Joint RFC, 91 Fed. Reg. at 37876, Question 11.

16 *See* Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554.

and would require meaningful modernization before it could accommodate perpetual structures, and any such modernization must be paired with safeguards commensurate with the leverage, continuous-trading, and funding-rate features that distinguish these products from the security futures Congress contemplated in 2000.

Perpetual contracts derive their pricing from intra-day movements in the underlying equity, rather than from close-of-day reference prices used in conventional equity derivatives. That timing distinction creates manipulation and volatility concerns for perpetual contracts that do not arise in connection with traditional equities or other equity-linked products. In addition, manipulative conduct in perpetual contract markets could ripple into the related equities and options markets, and such manipulation may escape detection unless all of these markets were subject to coordinated surveillance under a single regulatory authority.

In addition, any breakdown in the convergence of the perpetual contract price with the underlying spot price (whether from manipulation or a structural failure of the funding rate mechanism for a particular contract) could distort equity pricing in the broader equity markets in ways that impair not only secondary trading of securities, but also issuers' ability to raise capital. Parallel perpetual contract markets could also siphon liquidity from the traditional equity markets, raising concerns about undermining the capital allocation function of the equity markets. As with event contracts, the Commissions should consider whether migration of economically similar activity into perpetual contract markets could fragment liquidity, weaken price formation, or diminish the effectiveness of existing protections in the securities markets.

The Commissions also should evaluate whether the protections available under the security futures regime are sufficient for a product that is designed to track the spot price and that, in economic substance, more closely resembles a leveraged position in the underlying equity than a traditional future. At the same time, perpetual contracts involve counterparty credit exposure and margining obligations that are more characteristic of security-based swaps or security futures than of spot equity transactions. The regulatory framework applicable to perpetual contracts should account for the distinctive features of such contracts and afford appropriate customer protections.

In addition, many of the issues relevant to perpetual contracts on equity underliers apply with equal force in the commodity context, though several additional issues particular to commodity markets deserve attention. Price formation for many spot commodities occurs in thinly traded, decentralized markets with limited oversight. While perpetual contracts on such commodities may provide additional liquidity, manipulation or volatility in pricing in these spot markets could impact pricing in perpetual contract markets. Moreover, the pricing of traditional commodity derivatives reflects inputs, such as freight, delivery location, and warehousing costs and capacity, that the spot-market benchmarks used in connection with perpetual contracts may not fully capture. If perpetual contracts are priced off indicators that omit these factors, and perpetual contracts come to influence broader price formation in related commodity markets, the result could be systematic mispricing across commodity markets. MFA submits that, prior to approving a proposed commodity perpetual contract, the Commissions should carefully scrutinize the reference price methodology of such contract and ensure that these risks are mitigated.

Commodity derivatives markets exist in large part to serve end users looking to hedge a particular exposure, and pricing disruptions in perpetual contract markets could impair the ability of such end users to adequately hedge their exposures—with potentially serious consequences for the wider economy. In addition, as described above, the perpetual contracts that are available today generally trade on a 24/7 basis, and the Commissions should consider whether such 24/7 trading may disrupt the ability of market participants to properly engage in hedging activity. The Commissions should consider these limitations on the hedging utility of commodity perpetual contracts, as well as the potential for pricing disruptions to cascade from perpetual contract markets into the traditional futures and physical markets on which end users rely, when evaluating whether to approve perpetual contracts on specific commodity underliers.

The Commissions also should recognize the distinct risks introduced by 24/7 trading in commodity perpetual contracts. Where the underlying physical market is assessed only during defined trading windows, prices formed during off-hours may lack the liquidity and reliability needed to resist manipulation. If 24/7 trading is not appropriate for a given commodity underlier, those seeking to offer perpetual contracts on such underlier should be required to propose suitable trading hours and to explain how potential pricing dislocations outside those hours will be addressed.

### B. The Commissions should revise their interpretation of "compo" equity swaps

The Commissions have asked whether there is a need for greater clarity regarding the definitional lines between swaps, security-based swaps, and mixed swaps.[17] We respectfully request that the Commissions reconsider the mixed swap classification of compo equity swaps on a single security or narrow-based security index and align their treatment with that of quanto equity swaps - that is, as security-based swaps.

In the 2012 joint release entitled "Further Definition of 'Swap,' 'Security-Based Swap' and 'Security-Based Swap Agreement'; Mixed Swaps; Security-Based Swap Agreement Recordkeeping,"[18] the Commissions distinguished between quanto and compo equity swaps, classifying the former as security-based swaps and the latter as mixed swaps. A quanto equity swap provides an investor with currency-protected exposure to a foreign currency-denominated equity index by translating the percentage equity return in the foreign currency into domestic currency, using the prevailing exchange rate at the time the transaction is entered into.[19] With respect to quanto equity swaps, the Commissions classified such transactions as security-based swaps on the ground that the dealer's foreign exchange exposure is a byproduct of the hedging

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17 *See* Joint RFC, Question 3.

18 SEC and CFTC joint release, "Further Definition of 'Swap,' 'Security-Based Swap' and 'Security-Based Swap Agreement'; Mixed Swaps; Security-Based Swap Agreement Recordkeeping," 77 Fed. Reg. 48208 (Aug. 13, 2012). ("**Joint Product Definitions**").

19 Joint Product Definitions at 48265.

instruments it selects, rather than a feature of the swap's payment obligations, and that the currency component is merely “incidental.”[20] The Commissions also observed that where a total return swap references a foreign-currency-denominated security and the payout is computed by first determining the total return in the local currency and then translating the resulting amount into U.S. dollars at the then-prevailing exchange rate, the transaction remains a security-based swap rather than a mixed swap, even though such a transaction would not be a quanto swap.[21]

A compo equity swap, by contrast, exposes parties to the combined effect of movements in the referenced foreign stock and in the applicable exchange rate.[22] The Commissions classified compo equity swaps as mixed swaps, reasoning that because an investor could elect to enter into a quanto equity swap to avoid currency exposure, an investor's decision to transact via a compo structure makes the resulting currency component more than "incidental."

This difference amounts only to the allocation of the currency risk between the two parties. Under the quanto structure, it is the dealer that bears this risk; under the compo structure, it is the investor. The identity of the party to whom currency risk is allocated is not a sound basis on which to determine whether one or both Commissions exercise jurisdiction over a product, and it cannot justify classifying compo equity swaps as mixed swaps while categorizing quanto equity swaps as security-based swaps. A compo equity swap does not contain a separate derivative to “hedge” its currency exposure, nor is such exposure anything other than “incidental” to the party’s position in the underlying foreign-currency-denominated security. Indeed, the very rationale the Commissions invoked to classify quanto equity swaps as security-based swaps applies with equal force here: just as the currency component of a quanto swap is “incidental” because it is a byproduct of the dealer’s hedging, the currency exposure in a compo swap is “incidental” to the party’s position in the underlying foreign-currency-denominated security. Because the Commissions established this interpretation jointly in the 2012 release, they have the authority to revisit and correct it now, and no legislative change is required to do so.

The Commissions’ own prior guidance supports this correction. In explaining when interest-rate or currency terms convert a security-based swap into a mixed swap, the Commissions distinguished between terms that are merely a byproduct of, or incidental to, a party’s position in the underlying security and additional elements that create separate exposures unrelated to that position. The currency-translation feature of a compo equity swap falls squarely within the former category: it is inherent in taking exposure to a security denominated in a foreign currency, not a discrete foreign-exchange derivative appended to an equity swap. Reclassifying compo equity swaps as security-based swaps would therefore bring the Commissions’ treatment of these instruments into line with the economic-substance principle that the Commissions

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20 *Id.*

21 *Id.* at 48265, n.650.

22 *Id.* at 48265.

themselves have articulated, while eliminating an inconsistency that turns solely on which counterparty happens to bear the incidental currency risk.

The mixed swap characterization imposes substantial and unjustified compliance costs on MFA's members. Mixed swaps are subject to joint regulation by both the CFTC and the SEC, requiring dual compliance with the reporting, recordkeeping, and conduct obligations of both regimes. For a product that is, in economic substance, an equity swap with a currency translation feature—rather than a hybrid of an equity derivative and a foreign exchange derivative—this dual compliance burden is disproportionate to any regulatory interest served. This heightened regulatory burden increases the cost of transacting in these products, disincentivizing market participants and draining liquidity from the markets. Because MFA's members transact in these products on behalf of pension plans, university endowments, charitable foundations, and other institutional investors, these unwarranted costs are ultimately borne by those beneficiaries. Correcting the classification would remove a disproportionate burden on precisely the institutional participation that deepens liquidity and supports efficient pricing in these markets.

## III. Conclusion

Across each of the issues addressed in this letter, a common principle holds: a regulatory framework that protects responsible institutional participation ultimately serves the pension plans, university endowments, charitable foundations, and other institutional investors whose capital MFA's members manage.

To advance that objective, we respectfully urge the Commissions to (i) develop a framework for novel products that preserves comprehensive, coordinated surveillance and reserves to the SEC its role as the primary guardian of the securities markets; (ii) require the affirmative approval of both Commissions, in place of self-certification, before a novel product implicating each agency's interests is brought to market; and (iii) revise the mixed-swap classification of compo equity swaps to align it with the economics of those transactions and with the treatment of quanto equity swaps. Each of these measures rests on the same foundation: a framework that facilitates responsible institutional participation while insisting on robust governance, transparency, and surveillance will strengthen these markets to the ultimate benefit of the beneficiaries our members serve.

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MFA appreciates the opportunity to comment on the Joint RFC and commends the Commissions for undertaking this important and timely review. We would welcome the opportunity to discuss our comments in greater detail and stand ready to serve as a resource to the Commissions and their staffs as this work proceeds. Please do not hesitate to contact Matthew Daigler (mdaigler@mfaalts.org) or the undersigned (jhan@mfaalts.org) with any questions regarding this letter.

Sincerely,

/s/ Jennifer W. Han

Jennifer W. Han
Chief Legal Officer & Head of Global Regulatory Affairs
MFA

cc: The Hon. Michael S. Selig, Chairman, CFTC
The Hon. Paul S. Atkins, Chairman, SEC
The Hon. Hester M. Peirce, Commissioner, SEC
The Hon. Mark T. Uyeda, Commissioner, SEC