Submitted Electronically

February 21, 2025

International Organization of Securities Commissions
C/ Oquendo 12
28006 Madrid
SPAIN

Re: Public Comment on Pre-Hedging Consultation Report (November 2024)

Dear Sir/Madam:

The Securities Industry and Financial Markets Association Asset Management Group ("**SIFMA AMG**"), American Council of Life Insurers ("**ACLI**"), and Investment Company Institute ("**ICI**") (collectively, the "**Associations**") are submitting this letter on behalf of our respective members (the "**association members**") to address portions of the Pre-Hedging Consultation Report (the "**Consultation Report**") of the International Organization of Securities Commissions ("**IOSCO**").[1]

The Consultation Report appears to start from the assumption that pre-hedging should be permissible in a wide variety of circumstances, despite acknowledging that pre-hedging gives rise to certain risks including misuse of information, lack of transparency, and lack of client consent and understanding.[2] The Associations respectfully disagree with this assumption. Although we strongly support IOSCO's goal of providing recommendations that will set the standard for pre-hedging globally, we urge the adoption of recommendations guiding regulators in establishing clear boundaries to limit the practice to minimize the harm that can arise from dealers trading before their clients.

Pre-hedging involves a dealer trading ahead of a client based on information regarding an anticipated trade received from its client and, therefore, a dealer may only trade on such information with the client's express affirmative consent on a trade-by-trade basis following

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1 IOSCO, Consultation Report: Pre-hedging (November 2024) *available at* https://www.iosco.org/library/pubdocs/pdf/IOSCOPD778.pdf.

2 Consultation Report at 10-11. The Consultation Report cites two recent examples involving enforcement actions by the Australian Securities and Investments Commission and the U.S. Financial Industry Regulatory Authority. *See* Consultation Report at 15-16. In addition, the U.S. Commodity Futures Trading Commission ("**CFTC**") recently issued a consent order related to a swap dealer's practice of "pre-hedging" foreign exchange forward transactions. *See In the Matter of: Mizuho Capital Markets LLC, Respondent*, CFTC Docket No. 23-24 (Apr. 25, 2023). The dealer failed to disclose to clients that it would trade in the minutes or seconds prior to providing the spot exchange rate and executing the transaction, potentially moving the spot exchange rate against the client. As a result, "the client at times likely obtained the currency it sought to acquire via the foreign exchange forward at a rate less favorable than may otherwise have been available, and [the dealer] may have been able to hedge its exposure vis-à-vis its clients at a rate more favorable than may otherwise have been available." *Id.* at 1.

appropriate disclosure and only when it is designed to benefit the client. Trading without such express (and informed) consent allows a dealer in possession of such information to potentially negatively impact the execution of its client's trade, to the dealer's benefit, and indeed, allows the dealer to "hedge" a client transaction it may never engage in and a risk that it may never take on.

Although existing laws, regulations, and self-regulatory organization rules address market abuse and manipulation, including frontrunning, these regulatory regimes differ between jurisdictions. Pre-hedging must be specifically addressed by regulators. We believe, based on the key elements outlined above (appropriate disclosure, express consent and client benefit), pre-hedging is only appropriate in certain narrowly defined circumstances where the dealer takes on outsized risk in the anticipated transaction and the potential for harm to the client can be minimized (or at least, that it is knowingly consenting to any such harm and still wishes to proceed)—this would only include large, bespoke trades in over-the-counter ("**OTC**") illiquid markets where there is active collaboration between the dealer and client to accomplish the trade. Even in those narrow circumstances, the client should be able to decide whether to permit pre-hedging.

Below we address some of the questions raised in the Consultation Report. Throughout these responses, we emphasize the principles discussed above.

I. Definition

1. *Do you agree that this is the correct definition of pre-hedging? If not, how would you define pre-hedging? Does the definition of pre-hedging clearly differentiate it from inventory management and hedging?*

   We do not agree that this is the correct definition of pre-hedging because it conflates two concepts: (1) what pre-hedging is—a dealer trading ahead of a client's transaction, based on information about the anticipated trade received from the client, for the dealer's own benefit—and (2) when, if ever, such behavior should be permissible. Pre-hedging is simply trading undertaken by a dealer in a principal capacity where the trades are executed after the receipt of information about an anticipated client transaction and before the dealer and client have irrevocably agreed on the terms of the transaction. Jurisdictions have long recognized that behavior that meets this definition of pre-hedging could constitute market abuse, such as frontrunning. IOSCO should therefore distinguish between the concepts of "pre-hedging" and "permissible pre-hedging" as "permissible pre-hedging" would reflect a much smaller set of transactions and behaviors.

   With respect to the IOSCO's proposed definition, we agree that "pre-hedging" only occurs when the dealer is acting in a principal capacity (*i.e.*, prong (i)). There is never a need to pre-hedge when a dealer is serving in an agency capacity because the dealer will not take on any risk from the anticipated transaction. We would revise prong (ii) of IOSCO's definition to provide that pre-hedging occurs after the receipt of information about an anticipated client transaction and before *the dealer and client* have irrevocably agreed on the terms of the transaction. This change would make clear that any trading taking place before parties irrevocably agree to the terms of the transaction is pre-hedging, regardless of whether the client or the dealer is the one who finally accepts the terms of the trade. For example, the Consultation Report's definition does not account for situations where the dealer has a "last look." In this scenario, the dealer has sole discretion over whether to accept the client's trade and until such acceptance the client bears the market risk. A dealer that conducts any trading activity in the context of "last look" is pre-hedging because the dealer has not yet taken on any risk. Trading after the transaction has been irrevocably agreed to by both parties is, of course, actual hedging because it involves the off-loading of known risk held by an entity, here a dealer, in connection with its investments. In contrast, when a dealer "pre-hedges" it is reacting to a risk it does not bear but ostensibly believes it may or will. It may never actually receive or agree to the client transaction that it is pre-hedging and therefore may never take on the associated risk. A dealer trading before receiving information about a trade is mere pre-positioning and is generally acceptable as the dealer is not using the client's information to obtain a better price for itself at the client's expense.

Pre-hedging creates a conflict of interest between the dealer and the client and therefore entails certain risks and benefits that must be balanced in favor of the client. The primary risk is that the dealer's pre-hedging will negatively affect the client's price. The primary benefit of pre-hedging goes to the dealer who reduces the risk related to the potential client transaction, with little, if any, benefit to the client. Instead of pre-hedging, a dealer can always enter into a transaction with a client and then hedge the risk following execution. When a dealer pre-hedges instead, it ensures any price-slippage in the relevant market impacts the client's transaction, not its own hedge.

To prevent dealers from taking advantage of this lopsided risk-reward structure, we propose that IOSCO provide a recommendation defining what is "permissible pre-hedging."

First, pre-hedging must, of course, be in compliance with existing laws and regulations, including those regarding frontrunning. The Consultation Report acknowledges that "IOSCO has not analyzed when pre-hedging entails market abuse in different jurisdictions" but intends its recommendations to be "ancillary" to "existing regulations, including market abuse regulations."[3]

Second, a dealer should only pre-hedge after a client has given explicit informed consent in the context of a particular trade. The client itself is best situated to determine whether the benefits of pre-hedging outweigh the risks in the context of a particular transaction, and therefore explicit client consent (and, importantly, not "deemed" or "negative" consent) should be required before a dealer is permitted to pre-hedge the transaction. Associated with this is the need for appropriate and fulsome disclosure (as more fully described below).

Third, a dealer should only pre-hedge when it is designed to benefit the client.[4] This will help to increase the probability that pre-hedging results in a favorable risk-benefit outcome

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3 Consultation Report at 8.

4 The industry codes cited in the Consultation Report each include the concept of client benefit in their principles applicable to pre-hedging. *See* Global Foreign Exchange Committee, *FX Global Code* (rev'd Dec. 2024), *available at* https://www.globalfxc.org/uploads/fx_global.pdf (including within the definition of pre-hedging that the trades are "designed to benefit the client"); FICC Market Standards Board, *Standard for the execution of Large Trades in FICC Markets* (May 6, 2021), *available at* https://fmsb.com/wp-content/uploads/2021/05/FMSB_Large_Trades_Standard_-FINAL-05.05.21.pdf (providing that pre-hedging should only be conducted when "it is designed to benefit the client and not executed in a manner that is meant to disadvantage the client"); London Bullion Market Association, *Global Precious Metals Code* (Dec. 2022), *available at* https://www.juliusbaer.com/fileadmin/legal/global-precious-metals-code.pdf (including within the definition of pre-hedging that the trades are "designed to benefit the Client"). Not all SIFMA AMG members have signed on to these codes. We mention them not as an endorsement, but to emphasize the

for the client. Further, there is typically not only one way to hedge a given transaction and a dealer often has flexibility in how it pre-hedges, so this requirement would help to ensure that a dealer always considers the impact on its client when choosing among its options. Ultimately, this would help to minimize any negative impact on the price a client ultimately pays for a trade.

Accordingly, we recommend the definition be revised as shown below:

> Trading undertaken by a dealer~~, in compliance with applicable laws and rules, including those governing frontrunning, trading on material non-public information/insider dealing, and/or manipulative trading,~~ where:
>
> (i) the dealer is dealing on its own account in a principal capacity;
>
> (ii) the trades are executed after the receipt of information about an anticipated client transaction and before the dealer and client (or an intermediary on the client's behalf) ~~has~~ have irrevocably agreed on the terms of the transaction and/or irrevocably accepted an executable quote; and
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> (iii) the trades are executed to manage the risk related to the anticipated client transaction.

And we advise that IOSCO include a related recommendation that pre-hedging is permissible solely when:

> (i) it is in compliance with applicable laws and rules, including those governing frontrunning, trading on material non-public information/insider dealing, and/or manipulative trading;
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> (ii) it is designed to benefit the client; and
>
> (iii) the client has given its prior, affirmative and express consent to the dealer's trading prior to the execution of its anticipated transaction after appropriate and fulsome disclosure.

II. Genuine Risk Management Purpose

2. *Do you agree with the proposed types of genuine risk management? Are there other factors not mentioned in this report that should be considered for determining genuine risk management?*

We do not agree that testing market prices and liquidity is a type of genuine risk management. If a dealer is holding itself out to make a market in a particular security, it should generally have no reason to test the market for that security by pre-hedging. The dealer has other ways to assess the liquidity of the market, including monitoring its own order book, and should otherwise be attuned to market conditions affecting the liquidity of the relevant security.[5] In addition, there are many trades today with respect to which a

necessity of including that pre-hedging is designed to benefit the client in any recommendation defining permissible pre-hedging.

5 The Consultation Report's discussion of the factors that dealers should consider in determining whether there is a genuine risk management purpose does not recognize that dealers have ways to assess market liquidity other than pre-hedging.

dealer cannot pre-hedge (whether because of rules or market standards applicable to the trade or because the client has specifically prohibited pre-hedging of its trade). For example, when a dealer provides a firm bid and ask quote, it is required to enter into the trade at the quoted price immediately upon acceptance of the quote by the client; the dealer cannot pre-hedge because it does not know the direction the client will go nor can it pre-hedge once it does know the direction because it is required to execute the trade immediately. Yet dealers are still able to provide quotes for these and other trades, indicating pre-hedging is not actually necessary to test market liquidity.

Further, many jurisdictions provide for delays in trade reporting, affording dealers additional time to lay off risk after a trade has taken place but before the related information is public, obviating the need to pre-hedge.[6] As such, permissible pre-hedging should be reserved for trades that are far outside a dealer's typical market-making activities where a dealer would be exposed to significant risk in undertaking that transaction and hedging after the trade would not be sufficient to manage that risk.

We do agree with IOSCO's recommendation that in the narrow scope of permissible pre-hedging, a dealer would still need to determine whether there is a genuine risk management purpose for its trades. The factors listed in the Consultation Report, including (i) the dealer having a legitimate expectation of a client transaction; (ii) the available liquidity; (iii) current market conditions; and (iv) the extent of pre-hedging that is required (*i.e.*, proportionality), should still apply. However, these factors should not be weighted equally; for example, without the dealer having a legitimate expectation of a client transaction, pre-hedging should never be permissible. As noted below, we do not believe that pre-hedging should ever be permissible where there is competition to win a trade, such as a competitive request for quote ("**RFQ**") process (*i.e.*, an RFQ to more than one dealer), as when there is competition for the client's trade, no single dealer can assume it will win the trade. In such situations, a dealer cannot be said to have a genuine risk management purpose because the

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6 For example, the European Markets in Financial Instruments Regulation ("**MiFIR**") regime permits deferrals of post-trade publication of details regarding certain trades. *See Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012*, Articles 7, 11, 11a, 20, and 21. Likewise, in the United States, there is at least a 15-minute delay (depending on the type of trade) between the time at which certain swap transactions take place and the time at which they must be reported. *See* 17 C.F.R. § 43.5. In the adopting release for this rule, the CFTC noted that one of the reasons for the time delay was to provide market participants with adequate time to hedge their trades: "[C]ommenters asserted that the costs of risk management to end-users may increase if data relating to large sized trades is publicly disseminated to the market before swap counterparties have an opportunity to hedge a publicly reportable swap transaction." CFTC, *Real-Time Reporting of Swap Transaction Data*, 77 Fed. Reg. 1182, 1239 (Jan. 9, 2012). This example illustrates that dealers often are afforded reporting delays that allow them time to hedge after a transaction is executed. However, SIFMA AMG does not endorse the CFTC's sizing of the block trades subject to these delays, which has been criticized by industry participants. *See, e.g.*, Global Markets Advisory Committee, *New Block and Cap Sizes* (Nov. 6, 2023), *available at* https://www.cftc.gov/media/9606/GMAC_NewBlockCap110623/download (stating that the advisory committee to the CFTC "does not believe the new increases in certain transactions properly strikes the right balance between transparency and liquidity"); SIFMA AMG, Letter to Mr. Vince McGonagle, CFTC regarding Request for a delay to the compliance date for new Block Thresholds and Cap Sizes (Oct. 6, 2023), *available at* https://www.sifma.org/wp-content/uploads/2023/10/Request-for-a-delay-to-the-compliance-date-for-new-Block-Thresholds-and-Cap-Sizes.pdf (noting that SIFMA AMG members "firmly believe that with respect to many, if not most, product types, the magnitude of the planned increase in block size would have an adverse impact on liquidity with respect to existing block trades which would no longer benefit from RFQ to one and delayed reporting").

dealer's risk is far from certain—it cannot have a legitimate expectation of a client transaction.

III. Available Liquidity

3. *Do you agree that pre-hedging of wholesale transactions should be acceptable where there is sufficient liquidity in the underlying instrument/s to hedge after the trade is agreed to? Please elaborate.*

No. Permissible pre-hedging should be limited to large, bespoke trades in OTC, illiquid markets where there is active collaboration between the dealer and client to accomplish the trade. It should never be available where there is sufficient liquidity in the markets such that dealers would not need to pre-hedge in order to effectively manage their risk.

Where a market is sufficiently liquid, the dealer can lay off any risk related to the trade after the trade is agreed to. This includes situations not only where the market in the subject security is liquid, but also where the market for a related security is liquid. For example, in the context of a swap transaction, the dealer can hedge in the underlier, which may have a more liquid market, allowing the dealer to adequately lay off risk after the trade is executed. Further, in liquid markets, the dealer takes on less market risk, so there is less reason to pre-hedge in the first place. In these cases, the risk-management benefit to the dealer does not outweigh the negative impact on the price paid by the client.

In the case of OTC, illiquid markets, there may be more of a need to pre-hedge, as a dealer may rely on pre-hedging in order to even provide a quote for such a trade. We acknowledge that these trades expose the dealer to more risk than typical market-making activities in liquid markets, including that the dealer may not be able to lay off the risk of the trade completely after executing the trade. However, pre-hedging in such circumstances also has the potential to create the most negative impact to execution of the client's transaction and therefore express consent, as described below, is still absolutely necessary. From the client perspective, permitting pre-hedging only in these limited circumstances, taking into account the nature of the trades, would help ensure that appropriately knowledgeable personnel are involved in the discussions and therefore able to give informed consent to the dealer's pre-hedging.

4. *Can there be a genuine need to pre-hedge small trade sizes in liquid markets for risk management purposes?*

No. Although the risk of harm to clients is reduced for small trades and in liquid markets, so too is the dealer's need to pre-hedge for risk management purposes. Permissible pre-hedging should be aligned with the potential risk assumed by the dealer from the anticipated order and in the case of a small trade in a liquid market, the dealer assumes minimal risk. In addition, in this scenario a dealer can effectively manage its risk by hedging after agreeing to the trade.

IV. Proportionality of Pre-hedging

5. *Where a dealer holds inventory should they first consider using such inventory to offset any risk connected with an anticipated client transaction or should they be allowed to pre-hedge?*

Dealers should always first look to their available inventory to determine whether they need to pre-hedge at all and, if so, to what extent. As noted above, permissible pre-hedging should always be designed to benefit the client. If a dealer can minimize the potential for harm to the client by using some of its available inventory first, it should do so. Further, in obtaining client consent to pre-hedge, a dealer should be able to demonstrate that it has a legitimate need to pre-hedge, taking into account its existing inventory.

6. *What factors should dealers consider in determining the size of pre- hedging an anticipated client transaction (e.g., size, instrument type, quotation environment)? Should there be an upper limit for the pre-hedging amount? If so, what type of limits (e.g., percentage based, Greek based) are appropriate for consideration? Please elaborate your response in relation to bilateral OTC transactions and for competitive RFQ systems including those in electronic platforms.*

As noted above, if a client expressly consents to pre-hedging, permissible pre-hedging should be limited to bespoke, over-the-counter trades in illiquid markets. Assuming a client has agreed to permit pre-hedging of its trade, a dealer should consider the trade's asset class, currency, tenor, and size in determining its pre-hedging activity.

A competitive RFQ, including those on electronic platforms, does not allow for permissible pre-hedging because no dealer can assume it will win the trade. Permitting pre-hedging in such circumstances carries significant risk of adversely affecting a client's trade by negatively impacting market price. Further, as no dealer can be certain of winning the trade, pre-hedging cannot be said to be in furtherance of a genuine risk management purpose (because it has no legitimate expectation of a client transaction), as discussed above.

In addition, the Consultation Report notes that some market participants "do not believe that trade-by-trade disclosure is practical for competitive RFQs sent on electronic trading platforms, as these are largely executed by automated trading algorithms, and dealers may not have a direct relationship with clients."[7] As we have repeatedly emphasized, informed, affirmative client consent must be given before pre-hedging can be considered legitimate. Within the scope of an RFQ to a single dealer, it is practical for the dealer to obtain prior consent, and pre-hedging may be permissible depending on other factors such as the liquidity of the market and the size of the trade. However, a dealer should not be permitted to pre-hedge in connection with an RFQ in virtually any other context (*e.g.*, to more than one dealer) for the reasons outlined above.

V. Client Benefit

7. *Do you agree with the concept of client benefit described above?*

No. A dealer should be able to demonstrate the benefit to the client before engaging in pre-hedging so that the client can give affirmative, informed consent. For example, the dealer should be able to demonstrate that the client would benefit through improved pricing by disclosing the price without pre-hedging compared to the price with pre-hedging. If the benefit is that the dealer can execute the trade in the first place, the dealer should be able to demonstrate with specific disclosure what characteristics of the transaction would prevent

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[7] Consultation Report at 36.

the dealer being able to quote a price without pre-hedging. The client could then decide whether it will permit pre-hedging because the trade could not be accomplished otherwise.

8. *Do you believe that financial benefits derived from pre-hedging by the dealer should be shared with the client? What proportion of the benefit to be shared with the client would be fair? Please elaborate.*

   As we note in our response to Question 1, permissible pre-hedging should always be designed to benefit the client.

9. *Should pre-hedging always be intended to achieve a positive benefit for the client or is it enough that a dealer pre-hedges for its own risk management and does not detrimentally affect the client?*

   As we note in our response to Question 1, permissible pre-hedging should always be designed to benefit the client.

VI. Market Impact and market integrity

10. *Should dealers be able to demonstrate the actions they took to minimise the market impact of their pre-hedging trading? In the event of not entering the anticipated client transaction, are there any considerations for dealers to minimise market impact and maintain market integrity prior to unwinding any pre-hedging position?*

    Yes. Dealers should be able to demonstrate in the post-trade disclosure to the client (discussed below) the actions they took to minimize market impact and maintain market integrity. This would include the specific steps taken by the dealer to pre-hedge the transaction and whether the dealer looked to its own available inventory first to avoid market impact and harm to the client.

    There are certain circumstances in which the potential for market impact is so great that pre-hedging should not be permitted at all. In particular, pre-hedging should not be permitted when there is competition to win the client's trade. If multiple dealers engage in pre-hedging, they may negatively impact market price. For example, as we describe in our response to Question 6, pre-hedging is not appropriate in a competitive RFQ situation because the purpose of such an RFQ is to gather several competitive quotes so the client can choose which dealer it will work with, so no dealer can be sure it will win the trade.

VII. Policies and procedures

11. *Do you agree with this recommendation on appropriate policies and procedures for pre-hedging? If not, please elaborate.*

    We believe that dealers should adopt and implement robust policies and procedures to provide for the limited circumstances when they may engage in permissible pre-hedging, including expressly listing the factors a dealer needs to consider, and requiring affirmative, informed consent from clients prior to pre-hedging. In addition, the policies and procedures should expressly provide that pre-hedging must be designed to benefit the client.

VIII. Disclosure

12. *What type of disclosure would be most effective for clients? Why?*

We believe that generic disclosures regarding pre-hedging are not sufficient. Such disclosure buries important information about pre-hedging in voluminous disclosure that governs the terms of the transactions and therefore serves a different function than effective risk disclosure. We are concerned that such disclosure would not effectively convey the risks of pre-hedging. Instead, a dealer should provide upfront disclosure on a trade-by-trade basis that includes specificity about the trade and the reasons why the dealer believes it needs to pre-hedge. This disclosure should include information on risks of pre-hedging to the client, including reduction in liquidity and a negative effect on price. This specific disclosure will ensure that the client can provide informed consent on a trade-by-trade basis, as we discuss below. We believe this disclosure could take a variety of forms (*i.e.*, oral or written) so long as it is sufficiently specific for the client to provide informed consent. The dealer should retain records to demonstrate that disclosure was provided and informed consent was given by the client.

IX. Upfront disclosure

13. *Should upfront disclosure be applicable irrespective of factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication? Are there any key challenges for dealers to providing pre-trade upfront disclosures?*

Yes, our response to Question 13 is consistent with our response to Question 12 above. We believe there should be upfront disclosure with sufficient information for the client to provide informed consent.

14. *What should be the minimum content of any upfront disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions.*

Yes, our response to Question 14 is consistent with our response to Question 12 above. We believe there should be upfront disclosure with sufficient information for the client to provide informed consent.

X. Trade-by-trade disclosure

15. *Should trade-by-trade disclosure be proportional to factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication? What should be the minimum content of trade-by-trade disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions, in particular in electronic trading platforms.*

Trade-by-trade disclosure should be sufficient for the client to give its express, informed consent to pre-hedging in the context of the particular trade. What constitutes sufficient disclosure may very well vary from trade to trade, but the overriding principle should be that the disclosure allows the client to give informed consent.

16. *Are there any challenges or barriers to trade-by-trade disclosure in the context of competitive RFQs and in the context of electronic trading? If yes, please elaborate.*

Although there may very well be challenges to trade-by-trade disclosure in the context of competitive RFQs, pre-hedging is not appropriate in such circumstances, as we note in our response to Question 6. In the case of an RFQ to a single dealer, we do not believe there would be any significant barriers to trade-by-trade disclosure.

XI. Post-trade disclosure

17. *Would clients benefit from post-trade disclosures about the dealer's pre-hedging practices in a transaction?*

    Yes. A dealer should provide its clients with post-trade disclosure informing the clients of the pre-hedging trades and how those trades impacted the client. Post-trade disclosure is an important tool for clients to evaluate what information they need going forward and whether to continue to give consent in the future. In addition, dealers would be able to demonstrate in post-trade disclosure the benefits and costs of their pre-hedging activity to the client with specificity. To this end, post-trade disclosure can be standardized but would need to include both what pre-hedging took place and how the execution price of the client's trade may have been affected. For example, post-trade disclosure could include an indication of the market price when the client first approached the dealer about the proposed transaction, compared to the final execution price. In cases where pre-hedging may have been necessary for the dealer to execute the trade at all, the disclosure should communicate that fact, consistent with the dealer's disclosure to obtain the client's consent before it pre-hedged.

18. *Should the nature and form of post-trade disclosure be agreed between the client and dealer at the start of their engagement on an anticipated transaction and be proportional to factors such as the size and complexity of the transaction and/or other factors such as level of client sophistication?*

    No. We think post-trade disclosure could be standardized to include the items discussed in Question 17 and need not be agreed between a dealer and its client prior to every trade.

19. *Are there any barriers to post-trade disclosure? Please differentiate between bilateral OTC transactions, competitive RFQs and pre-hedging in the context of electronic transactions, in particular in electronic trading platforms.*

    We do not believe there should be any barriers to post-trade disclosure in the context of permissible pre-hedging for the same reasons discussed in Question 16.

XII. Consent

20. *Do you agree that clients should have the ability to explicitly inform the dealer that they do not want pre-hedging to take place in relation to a specific transaction (or revoke explicit or implicit consent to pre-hedging)? Are there any circumstances under which the dealer would not be obliged to follow the new client instructions? If not, what are the potential issues or risks to clients of this approach? Please elaborate your response to the question for bilateral OTC transactions, for competitive RFQ systems and for those in electronic trading platforms.*

    Yes, clients should have the ability to inform the dealer that they do not want pre-hedging to take place in relation to a specific transaction (and indeed should have to expressly affirmatively consent to any pre-hedging). A client may not believe that it will benefit from the dealer's proposed pre-hedging. And even assuming the client benefits, in many cases, a client may have reasons for not wanting pre-hedging to take place. For example, for large trades involving public companies, pre-hedging could reveal non-public information to the market before the client is ready for such disclosure to be made, allowing third-party actors engaged in frontrunning to also beat the client's execution to market. A dealer that pre-hedges a transaction against client instructions has engaged in frontrunning.

21. *Should dealers be required to obtain explicit prior consent to pre- hedge for certain types of transactions? Please elaborate your response to the question for bilateral OTC transactions, for competitive RFQ systems and for those in electronic trading platforms.*

Yes, as discussed throughout this letter, a dealer should always be required to obtain informed, express, affirmative consent from its clients prior to pre-hedging a particular transaction. Neither negative consent nor deemed consent is sufficient. A dealer is not required to engage in pre-hedging activity; it is a purely voluntary activity for the benefit of the dealer as principal. In most cases, the dealer does not need to pre-hedge to manage risk because the dealer can sufficiently hedge after it executes the trade. The client bears the risk of pre-hedging because pre-hedging will negatively affect the price the client receives for a trade. Therefore, the client should be the one to determine whether pre-hedging is permitted. In cases where the dealer believes that hedging after execution is not sufficient, the dealer should disclose this to the client up-front as part of its pre-trade disclosure and, if the client agrees that the dealer may then pre-hedge, the dealer should provide post-trade disclosure demonstrating the benefit to the client. If the client does not consent to the dealer pre-hedging, the dealer may decline to engage in the trade. What the dealer cannot do is trade on the basis of information provided by the client for the dealer's own benefit and with potential detriment to its client.

XIII. Post-trade reviews

22. *Should stand-alone post-trade reviews be conducted for pre-hedging? How would this improve supervision of pre-hedging activities? Could this review be also used to respond to client requests for post trade review of execution practices?*

XIV. Controls

23. *Do you think it is reasonable (in terms of costs and benefits) to require dealers to have internal controls to ensure differentiation between pre-hedging and inventory management?*

Yes. Pre-hedging is distinguishable from inventory management because a dealer has received client information about a particular trade. The dealer should have controls in place that govern the receipt of client information and that require affirmative client consent before permissible pre-hedging activities are engaged in. Dealers should also have controls related to the rest of our recommendations in this letter, including post-trade disclosure and the limited circumstances of permissible pre-hedging.

XV. Record-keeping

24. *What level of detail would be sufficient to have adequate records of pre-hedging activity to facilitate supervisory oversight, monitoring and surveillance?*

XVI. Industry codes

25. *Do you believe that the industry codes already meet some or all of the recommendations? If so, please explain in detail how.*

The industry codes are specific to certain asset classes, voluntary, and a result of membership. The Associations reiterate that there is a need for global recommendations applicable to regulators that address all transactions a dealer may wish to pre-hedge. Although pre-hedging is conducted against the backdrop of existing rules regarding frontrunning and other misconduct, client harm as a result of pre-hedging practices continues to persist. As we discuss throughout this letter, express, affirmative, informed client consent is paramount to ensure the risks and benefits of pre-hedging activity weigh in favor of the client. Not all industry codes provide the protections we discuss in this letter (prior consent, post-trade disclosure and requiring pre-hedging to be designed for the benefit of the client) and therefore are not sufficient.

On behalf of the Associations, we appreciate the opportunity to provide this letter in response to the Consultation Report. If you have questions or require additional information, please do not hesitate to contact William Thum at (202) 962-7381 or bthum@sifma.org, Madison Ward at (202) 624-2057 or Madisonward@acli.com, or Tracey Wingate at tracey.wingate@ici.org. [8]

Sincerely,

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/s/ Tracey Wingate

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[8] The Associations are grateful to Dalia Blass, Marie-Louise M. Huth, and Leanne M. Van Allen of Sullivan & Cromwell for drafting assistance and guidance on this letter.

Appendix – Description of Industry Association Signatories

SIFMA AMG - SIFMA AMG brings the asset management community together to provide views on U.S. and global policy and to create industry best practices. SIFMA AMG's members represent U.S. and global asset management firms whose combined assets under management exceed $45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds. For more information, visit https://www.sifma.org/committees/amg/.

ACLI - The American Council of Life Insurers is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. Ninety million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 280 member companies represent 94 percent of industry assets in the United States. Life insurers are significant end-users of derivatives for prudential asset-liability management. Life insurers use derivatives to hedge risks and to fulfill their long-dated obligations to policy and contract owners.

ICI - The Investment Company Institute ("ICI") is the leading association representing the asset management industry in service of individual investors. ICI's members include mutual funds, exchange-traded funds ("ETFs"), closed-end funds, and unit investment trusts ("UITs") in the United States, and UCITS and similar funds offered to investors in other jurisdictions. Its members manage $38.2 trillion invested in funds registered under the US Investment Company Act of 1940, serving more than 120 million investors. Members manage an additional $9.6 trillion in regulated fund assets managed outside the United States. ICI also represents its members in their capacity as investment advisers to collective investment trusts ("CITs") and retail separately managed accounts ("SMAs"). ICI has offices in Washington DC, Brussels, and London.