

23 September 2011

Letter to be submitted by e-mail to [cpss@bis.org](mailto:cpss@bis.org), and [OTC-Data-Report@iosco.org](mailto:OTC-Data-Report@iosco.org)

Reference: Requirements for OTC derivatives data reporting and aggregation, September 2011

Mr. Daniel Heller,  
Head of Secretariat, CPSS  
Mr. Masamichi Kono,  
Chairman, IOSCO Technical Committee

Dear Mr. Heller and Mr. Kono,

The World Federation of Exchanges (“WFE”)<sup>1</sup> welcomes the opportunity to comment on the CPSS-IOSCO report on requirements for OTC derivatives data reporting and aggregation. Since the G20 first called on regulated exchanges and clearing houses in 2009 to see what they could provide in terms of services in this area, member exchanges have been moving forward in close cooperation with the rest of the financial industry while liaising regularly with their supervisory bodies as requirements are developed.

Poor quality of information and faulty risk management of OTC derivatives contracts have been recognized as a significant source of the financial crises the world has been experiencing since 2007; WFE appreciates the efforts of officials in addressing these deficiencies. This consultation takes the work forward in its consideration of data requirements that are needed to get an overview of the entire marketplace.

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<sup>1</sup> WFE is a non-profit trade association of publicly regulated stock, futures and options exchanges operating worldwide. The Federation contributes to the development, support and promotion of organized and regulated securities and derivatives markets. WFE is an affiliate member of IOSCO.

Since the crises began to unfold, several large exchanges and independent clearing houses, which are associates of this Federation, have developed services for OTC derivatives, including trading, clearing, and reporting services. Great strides have been made in advancing in this business area, in particular in the area of credit default swaps.<sup>2</sup> New products and services offered by exchanges and clearers often take several years and more to build up significant volumes of business, and the beginnings of our industry's work in the OTC field have coincided with very difficult markets. The circumstances in which G20 called on exchanges to step forward were not the easiest, as CPSS and IOSCO no doubt appreciate. It therefore seems normal for WFE to view this as a process that will take many years.

Member exchanges and clearers have shared interests with governments in this area, and multiple reasons of their own for exploring the avenues OTC instruments might open to them: in the first instance, better information on OTC should enhance the stability of the world's financial system, restoring trust and encouraging the return of investment to the regulated marketplaces which remain central to the exchanges; and in the second, in developing new services to complement regulated exchange operations.

WFE has discussed plans and progress at several of its global meetings, and it has been monitoring progress being made. It commissioned an extensive survey on this topic in October 2010.<sup>3</sup> The consensus of those which have been exploring this new field has been to proceed rapidly but with caution: it will take time to gain experience in handling these off-exchange instruments without undermining the risk profile of existing businesses.

### **General comments**

WFE supports the CPSS-IOSCO Task Force recommendation that at a minimum transaction level data be collected, including the transaction economics, counterparty information, underlier information, operational data and event data. Clearly, mastery of the overall capital markets environment must be regained, and these data points are essential for completing the picture. Nevertheless, WFE considers that while trade repository ("TR") databases should have this additional information, managing and analyzing all these data in an effective manner by the regulators will be very difficult tasks to accomplish. The benefits of managing this information for complete risk assessment by capital markets supervisors are clear. But at this time, the WFE believes it necessary to develop more information on how the management of these extensive, complex data sets will be set up once the mandate for market participants to report to trade repositories has been established.

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<sup>2</sup> To cite but one example, between March 2009 and September 2010, ICE Trust cleared over USD 12 tr notion in credit default swaps alone. In ICE Trust's studies, they demonstrate that transparency has narrowed the ranges on prices for the more illiquid products, a result that could be generalized with a high degree of confidence across all exchanges and clearing houses advancing in this work.

The CPSS-IOSCO paper cites at length the description of the Trade Information Warehouse, a subsidiary of DTCC, which is an affiliate of WFE.

<sup>3</sup> Tabb Group, "The Global Risk Transfer Market : Developments in OTC and Exchange-Traded Derivatives." <http://www.world-exchanges.org/members-area/studies/tabb-study>

On the question of access to the data gathered, the CPSS-IOSCO Task Force itself still has questions which will affect significantly the value of this initiative when it comes into effect. WFE would anticipate both some difficulties and good possibilities for the marketplace if multiple trade repositories are disclosing information to the public. On the one hand, it will become clearer to all where there is a concentration of transaction information, and as in the regulated exchange environment this may lead to better pricing for participants dealing in such contracts; and on the other hand, multiple actors reporting can make it hard for market participants to get a good view of the broad picture unless regulators agree on international standards for aggregation of data.

WFE welcomes the initiative of promoting the standardization of the mechanisms of data aggregation across the TRs' universe. In a global market with TRs providing services across different jurisdictions and asset classes, the chances of having just one TR covering all jurisdictions and asset classes becomes highly unlikely – notably, both US and EU regulations will support the principle of having several trade repositories competing in their jurisdictions. Because of this, WFE foresees that in a multi-TR environment, the consolidation of the data would be essential for the market oversight authorities and the public to understand, as is noted in the CPSS-IOSCO paper as well.

At this time, WFE does not have a clear picture of how transaction reporting information is to be aggregated. The process will determine much of the outcome. Clearly, WFE would favor a common international approach to aggregation, and so provide the marketplaces with standardized and comprehensible information from jurisdiction to jurisdiction.

The extent of disclosure is likely to vary, with the authorities having the most complete picture. As to what data the market would need access to, WFE would support public disclosure of only very highly aggregated data providing a summary view of positions.

In a footnote on page 4 of the CPSS-IOSCO Report, it is stated that “in some jurisdictions reporting to a trade repository may also be used and/or become mandatory with respect to data related to transactions executed on regulated markets.” WFE would wish to learn more about the questions behind this note, and the direction in which this might go – it seems unclear what the further benefits would be given the added costs in assuring compliance. Exchanges already publish their transaction data, and any additional reporting would have to be done in a harmonized manner in order to be beneficial.

### **Data gaps**

Member exchanges responding directly to this inquiry would be best placed to share their recommendations. They have been gaining experience of these problems as they have begun to clear such instruments.

### **Support for development and implementation of an international legal identifier**

The CPSS-IOSCO Report highlights the governance points that would be inherent in creating a global body for establishing and then overseeing legal identifiers. In an area of business this detailed and on this scale, one that is open to conflicts of interest and legal questions in many countries, the problems will have to be solved one by one. The public interest must be upheld

first and foremost, and so this standards-setting body must, in WFE's opinion, be subject to independent public oversight just as global audit and accounting standards are.

### **Development of a standard international product classification system**

Because futures and options exchanges work on the basis of standardized products, and see the benefit to the investing public in doing so, this Federation welcomes the call in the CPSS-IOSCO report asking that OTC products be classified and standardized. The Federation notes the recommendation that this work be led by the industry in consultation with the authorities, but at the same time it would urge officials to stay very active in leading the debate, as for example in setting targets for OTC product standardization.

One essential reason for suggesting a balance between industry-led work and official involvement is that expertise in this field remains very narrow; the Report's citations underscore the point that there have been a limited number of actors involved in this work so far. As CPSS-IOSCO tries to draw OTC somewhat closer to the regulated capital market environment, they might well consider how to broaden participation in their working parties. Fresh perspectives might be especially warranted given the scale and complexity of the tasks.

### **Conclusion**

In many WFE member jurisdictions, outstanding OTC positions have been reported to the capital markets authorities to begin with, improving their ability to judge overall risk positions. What has been reported to the authorities has not necessarily been reported to the marketplace in its entirety. CPSS and IOSCO can look to those jurisdictions' authorities to evaluate their relative success in balancing public marketplace versus private contractual interests, and draw lessons from them.

In addition, it is important to remember some of the goals exchanges have set for themselves in this area,<sup>4</sup> in order to minimize systemic risk and to create a better functioning market. Above all, safety and integrity need to be ensured. To do so effectively requires:

- Maximum use of derivatives trading on organized markets
- Maximum use of central counterparties where trading on organized markets is not feasible
- Bilateral collateralization of derivatives exposure (preferably handled by a third party) when organized trading or the use of CCPs is not feasible
- Mandatory registration of open risk positions and reporting standards for all derivative contracts.

In remembering these guidelines and the overall objective of minimizing systemic risk, the proper use of TRs - and the data required for them - comes into a clearer view.

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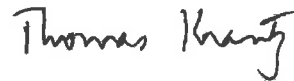
<sup>4</sup> Deutsche Boerse AG published a white paper in September 2009 entitled "The Global Derivatives Market: A Blueprint for Market Safety and Integrity." The objectives it set for guidelines would likely represent a consensus view among WFE members, as judging by the public discussions held on the subject at the last two annual meetings.

WFE welcomes further international consultation on what promises to be a long, complex but necessary process in providing reliable information on OTC trading.

Sincerely yours,



Ronald Arculli  
WFE Chairman  
Chairman of Hong Kong Exchanges and Clearing Limited



Thomas Krantz  
WFE Secretary General

Cc: WFE Board of Directors  
IOSCO Executive Committee Chairman Maria Helena Santana  
IOSCO Secretary General Greg Tanzer

## Annex: 2011 WFE Board of Directors

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