



*The Depository Trust &
Clearing Corporation*

CONSIDERATIONS FOR TRADE REPOSITORIES IN OTC DERIVATIVES MARKETS

Response by The Depository Trust & Clearing Corporation to the CPSS- IOSCO consultative report

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The Depository Trust & Clearing Corporation (DTCC) believes that repositories can play a crucial role to enable regulators and supervisors to address enhancing market transparency and reducing systemic risk.

The public benefit from information regarding (inter alia):

- the size and structure of the market
- open interest and turnover of positions

DTCC's experience with regulators and supervisors point to them valuing information regarding (inter alia):

- the size and structure of the market;
- positions and exposures of systemically important organisations;
- positions and exposures relating to failing or potentially failing institutions and their contagion impacts;
- concentrations in exposures in the markets;
- issues of potential market abuse, including understanding the impact of non-domestic transactions.

Furthermore DTCC believe that fragmentation is a key risk to the success of repositories (and therefore reform) in this regard, as in effect a fragmented localised model of data availability was the model pre-crisis. The OTC Derivatives Regulators' Forum has been very successful in establishing guidance for the Trade Information Warehouse (TIW) and enabling it to provide a complete perspective on the credit derivatives market to many international regulators.

Fragmented repositories (including any CCPs that may not elect to report to a repository) make the ability to produce consolidated information far more complicated and significantly less timely:

- Regulators will need to obtain data from multiple sources, and consolidate themselves;
- True market level concentrations may be diluted and less easy to detect
- The public may not have direct access to all the data necessary to provide a consolidated view;
- It may not be possible to create a full understanding of the net open position from multiple sources. The absolute values presented by net positions outputs are not necessarily additive;
- Obtaining data from multiple sources and consolidating the results will inevitably take longer than obtaining a consolidated report from a central source;
- Given the nature of OTC derivative products, in a multi-repository environment it is not always obvious which repository (or repositories) a given position should be registered in. Global rules will be needed to ensure that positions are neither omitted nor duplicated, and these rules implemented in firms at material aggregate cost.

The necessary level of oversight should be achieved by global co-operation between regulators from all continents, and through appropriate and agreed upon arrangements between regulators to share and guarantee access to data.

DTCC agrees, therefore, that it is important for trade repositories to operate in an international environment guided by international standards and welcomes the work of CPSS-IOSCO in this regard.

What is a Repository?

Within such a framework it is important that the functions and actions of a trade repository are clearly defined. To date, whilst there has been much discussion on the topic of repositories, there remains significant scope for different market players to interpret the term “repository” in different ways allowing scope for divergent offerings and varied levels of service.

Given this lack of definition, it would appear that providers have wide scope to determine what parts of their businesses and the depth of information that constitute performing “repository services” and therefore determine the applicability of the CPSS-IOSCO considerations for trade repositories in OTC derivatives markets. Specifically DTCC is concerned that the provisions around governance, linking, open access, transparency and efficiency should apply equally to all to the same degree. These standards should apply to equally to all repositories over equivalent data sets, including any “shadow repositories”, for example a CCP which is not reporting transactions to an independent repository. The G20 statements about derivatives as reiterated in the April meeting of Finance Ministers and Central Bank Governors in Washington, including the requirement for “reporting to trade repositories of all over-the-counter derivative contracts”.

DTCC believes that the functions of trade repositories (see appendix 1) are as follows:

- Position keeping
- Data validation
- Data cleansing
- Providing market transparency by through public reporting of aggregated trade data
- Providing market and firm position transparency to regulators through regulatory reporting.
- Enhancing the transparency of deal-books for participant firms

The lack of a clear definition means there are a number of other services that might potentially fall within the scope of a repository under the interpretation of some parties but which, in reality, are not repository services at all, for example:

- The provision of each contract with a unique identifier
- The provision of non-economic data to regulators, for example performance metrics of market participants (submission timeliness, accuracy, confirmation lags etc), or details of trade status's at specific points in time.

The functions and structure of the OTC markets is complex and DTCC believes that a clear and concise definition of a repository is key to ensuring regulators and other supervisors are able to rely on these key pieces of infrastructure to meet their ongoing transparency requirements.

Non-Repository Services

There are also many other ancillary services that are relevant to OTC derivatives processing such as trade compression services, clearing services, asset servicing, payment calculations and settlement processing that would clearly fall outside the scope of the trade repository services listed above. Such ancillary services should be considered separate to repository services and should be provided under the appropriate regulation and standards applicable to those services rather than being considered directly part of the repository services.

DTCC believes that the provisions of section 3 of the consultative report, subsection 8 – “Risks in links” – provide important context. DTCC's experience in operating the Trade Information Warehouse for credit derivatives indicates that data used for operational processes is generally of higher quality than data provided solely for reporting purposes. Therefore, the provision of ancillary services to a trade repository should be considered desirable. Where such ancillary services are provided by a different provider to that which provides the repository, we believe that the risks inherent in the design and operation of such links should be managed prudently.

Who should report to a repository

Given the global nature of the OTC markets, as well as the fact that there will be a mix of centrally cleared and non-cleared positions within the portfolios of market participants, DTCC believes that all trades – whether centrally cleared or not – should be reported to a repository. At times of market stress, having all positions reported to a trade repository will greatly reduce systemic risk by ensuring regulators can see a firm’s underlying position data and exposure from a central vantage point.

DTCC’s experience from events such as the Lehman bankruptcy and the market stresses surrounding Greek debt highlights the importance of this central view. The data required by regulators and other supervisors in such events is complex. Furthermore, the data requirements also tend to change over time as the particular events evolve. Providing such data from a central source ensures that it is provided in a consistent timely manner rather than being pieced together from numerous submissions from any number of separate repositories and CCPs.

DTCC believes that there is benefit in the majority of positions in a repository being reported by both counterparties. Generally, where both parties report the transaction, there will be a general improvement in the quality of the underlying data from which the reports are produced.

In general, industry participants and regulators are keen to see more automation and operational efficiency in OTC derivatives markets, and we believe that will mean electronic connectivity for most participants. In that context, submission of trade information to repositories should be relatively easy and can often be performed alongside another service, for example electronic confirmation, or it can be supported at low effort by affirmation in web portal interfaces. In addition it should be recognised that the products themselves are relatively sophisticated and hence the customers themselves will have a level of sophistication - OTC derivatives are not a retail product. Therefore we believe that reporting by both parties to a trade is both possible and desirable, but should permit the use of agents where necessary. To the extent that any proportionality is considered, we suggest this exclusion should be applicable to private individuals only. To avoid excessive costs of linking to a repository, a submission method with low cost to customer implementation must be provided.

Specific comments on proposed factors

1. Legal framework

DTCC agrees that a TR should operate in a clearly defined legal framework. However, given the central importance of TR’s in the OTC derivatives market infrastructure, DTCC also believes that this legal

framework should ensure that the principle of open-access applies equally to all providers of repository services.

The legal framework should also facilitate data sharing, ie ensure that data confidentiality provisions within the terms agreed between provider and customer do not impact but rather enable the ability to respond to regulatory and governmental enquiries.

Also, whilst a TR's rules, procedures and contractual arrangements should ensure that otherwise valid contracts cannot be invalidated through the TR's recording process, this shouldn't preclude all updates by the repository provider to reflect legally valid changes to terms. Note that DTCC believes that the maintenance of legal records of trades is an ancillary service, not a core repository service.

2. Market transparency and data availability

DTCC agrees that all TRs should make publicly available aggregate data on open positions and trading volumes on a periodic basis. This must be without disclosure of any parties position, as this is market sensitive information. Therefore, this data should be constrained with the proviso that, due to the structure of the markets in certain jurisdictions, there may issues surrounding unintended disclosure.

By way of example, in some markets there may only be one (or a small number) of major market players such that by publishing data on that geographical basis, other market participants may be able to understand the likely positioning of that market player. TR's should therefore first give consideration to whether the data being published gives rise to unintended disclosures, whether explicit or implied.

4. Governance

DTCC agrees that repository services should be developed to meet the needs of market participants including buy- and sell-side as well as regulators and other supervisors. As such, it is important that the industry governance groups are involved in the development of the scope of such services. With regard to the specific governance of a repository provider, this is a separate matter to the definition of industry requirements. Provided that industry and regulatory/supervisory requirements are met, the formation of the governance committee within a repository provider should also take into account matters such as the economics of service provision and therefore ensure the fee paying parties interests are represented, given many of the requirements will be determined by regulation.

5. DTCC agrees that the mission of a TR should be to aim to fully support the market's needs for recording trade information and reporting on OTC derivatives transactions. TR's should therefore aim to be able to

record all transactions within an asset class irrespective of the counterparties to those transactions.

DTCC fully supports open-access to TR's and agrees that one criteria for denial of access should be on a risk-related basis. However TR's other factors are also relevant:

- The service provider requesting access should be providing a service relevant to the repository or on behalf of one or more of the market participants that use that repository;
- Such a service provider has the consent of those market participants for whom it is providing a service to access the customers data;
- The service provider has the ability to meet standards required by the repository, including completeness of records and, where necessary, legal validity of submitted records.
- Ensuring that confidentiality laws are not breached through the granting of such access.

6. Safeguarding of data

DTCC believes that the liability of TR's is a complex multi-faceted issue. Matters such as the scope of data held and the products covered will have an impact. Therefore DTCC believes that the issue of liability is one to be agreed between the users of a repository service, the provider and also the regulators of that repository. DTCC also believes that insurance schemes are not the only way in which to manage liability and, therefore, recommends that the 3rd bullet point in section 6 of the considerations is deleted.

9. Communications procedures and standards

Whilst DTCC agrees that consistent communication procedures and standards are desirable, we also wish to point out that in a number of areas (such as counterparty naming) there are no such standards in existence and in others (for example underlying entity identification) there are multiple standards in existence.

Therefore, DTCC understands the desirability of using standards where they exist and where they are unique, but believes that the factors contained within this section of the considerations are too detailed.

Where a repository provider undertakes proprietary work in the absence of a standard, there should be no obligation to share this work freely with other providers of repository services

10. Efficiency

DTCC is supportive of unbundled pricing as a general policy. DTCC also is supportive of pricing policies that are reflective of costs, ie that do not reflect other cross-subsidies or loss leadership in their provision.

Additionally, there are some features of TIW that are worth referencing, in the context of efficiency:

- information derived from records maintained for operational processing is of a higher quality than that just used for reporting purposes only, and in providing data publicly and to regulators, data quality is of key importance to a repository
- The capability for TIW to provide regulatory and public reporting came at very low marginal cost to the capabilities required to service contracts. The vast majority of the market participants do not pay anything for any of the TIW services including repository services, and the fee paying participants have a strong role in governance and manage the cost of service provision and the pricing directly.

DTCC thinks that this model is of significant overall value in providing a service such as this on an efficient basis.

DTCC believes the recommendations would benefit from additional guidance on how quality of data in a repository may be ensured, eg by pre-matching in another service, matching in a repository, customer affirmation of data, official legal record keeping, and operational processing, or other reconciliation methods.

DTCC recommend that more context is given to the guidance as to the appropriate purpose, scope and participants for repository services, to make such a service identifiable and therefore the recommendations applicable.

Appendix 1 - Functions and Characteristics of a Trade Repository

A repository occupies a technical space in the global OTC derivatives trading environment. DTCC – through the Trade Information Warehouse’s global trade repository - supports the needs of the industry and regulators to hold, record and update information on OTC credit derivatives transactions from CCPs and more than 1700 market participants worldwide. In addition, the TIW connects to other service providers and acts as a hub for the exchange of trade information and other relevant data.

The TIW also provides a comprehensive operational infrastructure for CDS which is significantly over and above a reporting “repository” offering.

Among the TIW complementary functions for CDS as an adjunct to the trade repository include:

- Asset Services/lifecycle and event processing
 - Complete, up-to-date legal record keeping
 - Provision of a unique central identifier for each position

- Standardising treatment of identical cleared and non-cleared contracts
 - Supporting novation of contracts to CCPs
 - Enabling participants to assign (change ownership of) contracts electronically
 - Managing life cycle credit events (for example, bankruptcies)
 - Managing other life cycle events (for example, re-organisations and renames)
- Settlement Services
 - Calculating and netting cash flows
 - Managing custodian workflow for asset managers
 - Calculating payments and conveying instructions to payment systems for settlement in multiple currencies

DTCC agrees with the comments in the European Commission Staff Working Paper accompanying the Commission Communication, “Ensuring efficient, safe and sound derivatives markets” (SEC 2009) 905 final, 3 July 2009) highlighting the different fundamental natures of the OTC derivatives asset classes.

Therefore, for other asset classes (such as interest rates, equity derivatives, commodities, etc.) the nature of the products will dictate the overall operational infrastructure. For example, life cycle credit events are only relevant to CDSs.

DTCC therefore agrees that repository services that fall broadly under:

- 1) Position recording
- 2) Data cleansing
- 3) Reporting to regulators, the public and participant firms

should be provided on a global basis for each OTC asset class. The stated goals of a repository – “to foster transparency, thus supporting the efficiency, stability of and orderly functioning (i.e. avoidance of abusive behaviour) of financial markets” – are readily achieved through these services.

However, DTCC does not believe that it is appropriate to extend the definition of a repository to encompass the aspects of Asset Services (including legal record keeping) and Settlement Services that the TIW provides to the CDS market. These additional services are provided in addition to the trade repository and are complementary to it, as opposed to being an integral part.

Appendix 2 - About DTCC

The Depository Trust & Clearing Corporation (DTCC) brings considerable experience and expertise in the operation of critical post-trade market infrastructures to this discussion. DTCC has a nearly 36-year history of acting as a market-neutral provider of clearing, settlement and depository services to

the financial services industry. The organisation is owned and governed by our members and operated on an “at cost” or not-for-profit basis. DTCC is the product of 20 years of consolidation effort among multiple, competing central counterparties (CCPs) and central securities depositories (CSDs). Our central depository provides custody and asset servicing for 3.5 million securities issues from the US and 117 other countries and territories, valued at \$27.6 trillion. In 2009, we settled more than \$1.48 quadrillion in securities transactions.

Today, DTCC’s customers are increasingly global financial institutions which are headquartered in Europe as well as in the US and handle globally-traded instruments. In response to these changes, DTCC is, more and more, developing services to accommodate global regulatory requirements, and now encompass a networked community of thousands of financial firms in dozens of countries.

Throughout its history, DTCC has brought safety, soundness, risk mitigation and transparency to the financial markets. As an example, following Lehman Brothers’ bankruptcy last year, DTCC played a significant role in unwinding over \$500 billion in open trading positions from trades in equities, mortgage-backed and US government securities, without any loss to the industry – and saved taxpayers from shouldering an additional burden. We also have a history of working closely with regulators, especially during crises, to support their need for transparency and trade data to assess and mitigate operational, market and systemic risk more effectively.

DTCC has been present in Europe since 1995 and today provides a number of services in Europe. Through our subsidiary, EuroCCP, we are one of the leading pan-European central counterparties in the equities market. In addition, DTCC’s Fund/SERV mutual fund processing system has provided support to cross-border trading in investment funds (Luxembourg and Dublin funds) for nearly a decade. And its Global Corporate Action Validation Service supports firms in Europe, and around the globe, in providing a single source of validated corporate action data.

DTCC’s Trade Information Warehouse (TIW) – launched in 2006 – marked the first time that the financial services industry had addressed OTC derivative inventory control and transparency systematically. TIW provides a central automated repository to house and service virtually all credit default swap (CDS) contracts.

At the height of the Lehman Brothers crisis, TIW held a large proportion of the information on CDS positions written on Lehman debt. Although market speculation put the CDS risk exposure from Lehman Brothers at \$400 billion, DTCC was quickly able to tell the market publicly that the true exposure to Lehman Brothers was closer to a net notional value of about \$6 billion. The actual value that changed hands eventually was \$5.2 billion. Since then, TIW has been publishing aggregated OTC derivatives data for the public on a weekly basis on the website www.dtcc.com, and has been providing

regulators in the Americas and Europe information which they require, with the agreement of the market participants where necessary.