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RESPONSE OF THE FEDERATION OF EURO ASIAN STOCK EXCHANGES (FEAS) TO IOSCO-CPSS REPORT ON REQUIREMENTS FOR OTC DERIVATIVES DATA REPORTING AND AGGREGATION

Executive Summary

Below we provide a selective summary of our responses to the various sections of the consultative report

- Data aggregation and interconnectivity for OTC Derivatives on a global basis is a key success factor for trade repositories
- Standardized Reporting needs to be defined in a common language across markets
- Legal Entity Identifiers (LEIs) should be established on a global basis
- Product Classification should be undertaken by the industry and accepted globally
- Systemic risk models should be further discussed

General Remarks on OTC Derivatives Data Reporting and Aggregation Requirements

Global policymakers have released a set of recommendations for trade repositories that would collect consolidate and share data on over-the-counter (OTC) derivatives trading. The Committee on Payment and Settlement Systems and Technical Committee of the International Organization of Securities say they support the view that by collecting data centrally Trade Repositories (TRs) would provide the authorities and public with better, more timely information. “This would make markets more transparent, help to prevent market abuse, and promote financial stability,” they say.

The CPSS-IOSCO report proposes data requirements and formats that would apply to both market participants reporting to trade repositories and to trade repositories reporting to the public and to regulators. The report also finds that certain information currently not supported by trade repositories would also be helpful in assessing systemic risk and financial stability, and discusses options for closing the current gap in data.

It also discusses issues relating to data access for the authorities and report entities, including tools that could provide the authorities with better access to data and advocates a system of standard legal entity identifiers as an essential tool for aggregation.

Finally, the report calls for the industry to lead the development of a standard classification system for OTC derivatives products.



Trade Repositories as a Concept for tracking OTC Derivatives:

FEAS supports interconnected TRs on a global basis. Financial authorities in the US and Europe have advocated the introduction of a central trade repository to gather data on the (OTC) derivatives market, but there is concern that country-specific multiple repositories could do more harm than good. Further, there are concerns that separate facilities across markets would risk missing the bigger picture, as trades might be reported to multiple repositories or left unreported. Another concern is that it will be difficult for a repository to gather all of the trade information from across the OTC derivatives market, given the huge number of participants and in some cases the low levels of automation.

Designers of any repository will also have to determine which institutions would be mandated to supply trade data. It has been suggested that this shouldn't apply to banks only, as that would risk missing systemic problems relating to insurance companies and hedge funds (and other entities such as BCNs, dark pools, proprietary traders). But the inclusion of other entities will require the co-operation of regulators across not just geographical, but also sector lines. It seems necessary that there should be a repository for each underlying asset class globally. The construct may even be extended to cover a broader range of instruments, including cash, because if you look at the bond market, for example, the majority of activity is traded OTC.

While the concept of a trade repository is not controversial, there are issues to address; such as the recent explosion of repository providers is leading to fragmentation. It should also be noted that multiple repositories may lead to double-reporting, while others highlight the implicit problem of dividing repositories along asset-class lines.

The trade repositories may not reveal the picture in its fullest context as they will not be able to show positions across organizations. This problem may be partially addressed by developing interconnectivity between the different trade repository providers. Interconnectivity would help build a full regulatory picture but would still afford dealers a choice of reporting venue. In order for interconnectivity to be possible, the technical aspects of how to capture and extract data would have to be standardized in order for data to be properly reconciled and understood by the regulators. In the case of some existing TRs, the electronic confirmation of the trade is deposited and used as the “golden record” for that trade. However, other TRs are a database of input trade data. These are two distinctly different approaches.

Information Collected

A common LEI and product classification system will be a powerful tool for regulators in monitoring and managing systemic risks. With the employment of the LEI and product classification, data aggregation and analysis is more efficient, eliminating the need for cross-referencing and mapping when combining multiple data sets. It allows for much more powerful modeling and risk analysis and permits information sharing & reconciliation. Common identifiers for both the companies and the products will make it easier to share information on legal entities and their positions between regulators and across borders it allows



for better supervision of cross-border firms and firms whose business lines are overseen by multiple regulators. Further, the identification of Affiliates and Parent Companies means it is easier to make connections between parents and affiliates, especially when combined with basic hierarchy data; this in turn gives a deeper view into the company and a more holistic understanding of their overall positions whether they be long or short.

Further advantages for Risk Management such as a holistic view of counterparty risks will provide for easier data aggregation, modeling, analysis and the development of “Living Wills”. Other operational benefits to the industry include an integrated view of entities across divisions, development of hierarchy information, processing & settlement efficiency, and better corporate actions management.

Information to be furnished to trade repositories comprises the description of the details of a transaction. There has to be sufficient information to allow the calculation of a risk at the level of a central counterparty. Where a transaction of a counterparty subject to the reporting requirements of the proposed regulation cannot be processed by a trade repository, it could in turn be reported directly to the regulatory authority. Firstly, the actual entities must be uniquely identified concurrently; the trades must then be also uniquely identified (throughout their life cycle). Finally, the language of reporting must be standardized. Such a language clearly benefits from the work done for Credit Default Swaps (CDS) and Interest Rate Swaps (IRS), but also from efforts related to the FIXML protocol used for trade reporting and other purposes. A unified reporting standard for trade information may be the biggest contribution of the proposed regulation to achieve a reduction of systemic risks.

Measuring and aggregating risks

Provided all transactions have been reported in an easy to process format and attributed to a uniquely identifiable risk-bearing entity, this still leaves the issue of arriving and aggregating risk positions. Establishing the market value of a transaction, the ability to subject this value to various risk scenarios and to gauge the degree to which other positions can provide risk reduction effects requires a sophisticated risk engine. A trading repository does not imply automatically the existence of such a risk engine. Without the existence of a CCP, regulators interested in aggregating and analyzing risks already at the level of the trade repository, would either have to establish an own risk-engine or alternatively charge the trade repository to provide (or contract for) one. The aggregation of risk not just within a single CCP (and thus derivatives class) but across multiple types of derivatives will pose additional challenges.