

September 23, 2011

Committee on Payment and Settlement Systems and
Technical Committee of the International Organization
of Securities Commissions

Submitted via email to
cpss@bis.org and OTC-Data-Report@iosco.org

Re: CPSS and IOSCO Report on OTC derivatives data reporting and aggregation requirements

Ladies and Gentlemen,

Markit¹ is pleased to submit the following comments to the Committee on Payment and Settlement Systems and the Technical Committee of the International Organization of Securities Commissions (“**CPSS/IOSCO**” or “**Committees**”) on their consultative report on OTC derivatives data reporting and aggregation requirements (the “**Consultative Report**”).²

Introduction

Markit is a service provider to the global derivatives markets, offering independent data, valuations, risk analytics, and related services for these products across many regions and asset classes in order to reduce risk, increase transparency, and improve operational efficiency. Markit supports the objectives of the G-20 commitments³ and the Committees’ efforts of harmonizing international regulatory standards, as well as their initiative to identify and address data gaps that might prevent the creation of sufficient transparency for regulators in the OTC derivative markets.

Executive Summary

Significant progress has been made in establishing Trade Repositories (“**TRs**”) globally that capture accurate position and/or transaction information for OTC derivatives across asset classes. However, as the Committees noted, gaps may still exist in relation to the information and tools that are available to regulatory authorities which might prevent such authorities from making full use of the TR data.⁴ Specifically, regulators seeking to transform the notional positions of OTC derivatives that are captured in TRs into actual risk measures in order to monitor counterparty exposure or the level of interconnectedness in the financial system will need access to information about the current market value of these positions.

¹ Markit is a financial information services company with over 2,200 employees in North America, Europe and Asia Pacific. Please see www.markit.com for additional information.

² Report on OTC derivatives data reporting and aggregation requirements (24 August 2011).

³ “Leaders’ Statement: The Pittsburgh Summit” (Sept. 24-25, 2009) and “The G-20 Toronto Summit Declaration” (26-27 June 2010) available at http://www.g20.org/pub_communique.aspx.

⁴ CPSS/IOSCO identified existing data gaps as (i) accurate valuation data, (ii) bilateral portfolio data (e.g. net notionals based on aggregation, netting, master agreements, collateral, and margin information), and (iii) collateralisation (depending on nature of collateral, valuation, custody, legal framework).

CPSS/IOSCO's report highlighted several challenges to providing regulators with access to current market values for OTC derivative positions.⁵ The Committees also requested comment on the business, operational, and technological challenges entailed in providing this type of data to regulators via TRs or any other means.⁶

We believe that, when beginning to bridge gaps in valuation data for OTC derivatives, data should be both obtained from and communicated through reliable sources. Comparison between various options should be guided by how one can achieve the regulatory objectives in a timely fashion, whether the means of communication used are sufficiently secure and efficient, and how the creation of unnecessary cost for market participants and TRs can be avoided. As further explained below, we believe that these objectives can be best achieved if: (1) counterparty marks are used to address the data gap relating to current market values for OTC derivatives; and (2) TRs collect these counterparty marks and provide them to regulators.

Further, in relation to CPSS/IOSCO's questions on Legal Entity Identifiers ("**LEIs**"), we believe that: (1) the introduction of LEIs must build on global support and should be phased-in; (2) governance, operation and compilation of LEIs should be inclusive to reflect the views of all stakeholders; and (3) easy-to-use mechanisms need to be provided that permit market participants to obtain legal entity identifiers ("**LEIs**") through a self-registration process or from a counterparty who would act as their agent in the registration process.

Comments on Gaps in Valuation Data

1. The Data Gap Related To Current Market Values Can Be Best Addressed Through The Use of Counterparty Marks

For centrally cleared OTC derivatives, we believe that the daily settlement price provided by CCPs is an appropriate measure of current market value for regulatory purposes.⁷ However, for those OTC derivatives that are not centrally cleared, it is less clear where to source current market values from. It could be sourced, for example, from the counterparties to the transaction, from independent valuation providers, or from other sources.

In the Consultative Report, the Committees appear to view the provision of valuations by counterparties to TRs as the most natural approach. However, the Committees also indicated some concerns about the operational feasibility of this approach.⁸ We believe that counterparty marks should indeed be the preferred source of current market values for regulatory purposes, and address each of the Committees' concerns below:

a. Operational challenges

The Committees stated that it would be operationally challenging for all counterparties to submit their valuations to TRs, and for TRs to collect valuation information from a large number of counterparties.⁹ We believe that this would be true where parties do not regularly communicate daily marks to their counterparties, and where smaller counterparties like end-users are required to communicate their marks. However, these operational challenges may not be generally prohibitive based on the following:

⁵ The report states that a) the submission of this information by firms is complicated by the fact that the relevant information is often stored in several separate systems, b) the counterparties' valuations for a transaction might differ, and c) the required frequency for the provision of these valuations (which might be daily) could create significant operational challenges, risks and costs both to TRs and to participants. See Consultative Report, 14.

⁶ As CPSS/IOSCO mentioned, such alternative sources of information could include systematic assessment, CCPs, direct reporting from financial institutions, or information generated from alternative reporting schemes. See Consultative Report, 16.

⁷ Of note, these prices are also exposed to a high degree of regulatory scrutiny.

⁸ See Consultative Report, 14-16.

⁹ See *id.* at 14 ("the timely and frequent submission of such data may present significant operational challenges, risks and costs to TRs and participants.").

- Today, most major counterparties in the global OTC derivatives markets already provide many of their counterparties with marks for a significant number of their outstanding transactions. This generally happens on a voluntary basis. In addition, proposed regulation in the United States¹⁰ and potentially elsewhere will *require* all of the major market participants¹¹ to provide their counterparties with marks for *all* uncleared swaps and security-based swaps on a *daily* basis. Therefore, we believe that the communication of marks by counterparties is or will be an established process.
- The major market participants as well as various service providers have created mechanisms to deliver marks in an efficient, secure and auditable fashion, and these means are actively used today.¹² We believe that such established and robust infrastructure for the communication of marks to counterparties could be easily leveraged to communicate counterparty marks also to TRs.
- We agree that a requirement for *both* counterparties to each OTC derivatives transaction to provide their marks to the TR could impose a significant additional operational burden on some end-users or smaller buy-side clients. These entities might not currently mark their positions on a regular basis and might not have established connectivity with efficient delivery mechanisms for counterparty marks. The Committees might therefore consider requiring the provision of counterparty marks to TRs from the parties who are best equipped to do so.¹³ Such approach would minimize the incremental operational burden on participants, yet we would not expect it to result in significantly reducing the quality of the marks.

b. Differences between valuations

The Committees expressed concern over the potential for counterparties to provide different valuations for the same transaction.¹⁴ However, we believe that differences between counterparty marks, if any, might not be that significant, and the issue could be further addressed by requiring TRs to establish appropriate policies:

- Counterparties to an OTC derivative transaction are individually responsible for the valuation of their position. They might therefore indeed produce somewhat different marks for the same position given variations in their inputs and valuation methodologies. However, many counterparties currently identify and resolve valuation differences between them through regular Portfolio Reconciliation procedures already. In addition, proposed regulatory requirements will impose an *obligation* on many counterparties to resolve any significant valuation differences in a timely manner.¹⁵ We therefore believe that any remaining differences between counterparty marks will be only temporary or small.
- Further, we believe that CPSS/IOSCO should consider requiring TRs to establish policies and procedures to create a single mark in case they received several different ones for a position. This could, for example, be

¹⁰ See Section 764(h)(3)(B) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010); Business Conduct Standards for Security-Based Swap Dealers and Major Swap Participants, 76 Fed. Reg. 42396 (published 18 July 2011); Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties, 75 Fed. Reg. 80638 (published 22 December 2010).

¹¹ *I.e.*, Swap Dealers and Major Swap Participants

¹² *E.g.*, Markit Valuations Manager, a web-based platform that provides buy-side clients with the aggregation of counterparty position and mark data in a secure, auditable, timely and consistent format. This data is downloadable and easily fed into downstream systems, herewith streamlining workflow and saving significant time and cost.

¹³ These could, for example, be those counterparties that are obliged to communicate marks to their counterparties already, or those that are responsible for reporting the actual transaction to the TR at the time of execution, *i.e.*, the Reporting Party. See Regulation SBSR: Reporting and Dissemination of Security-Based Swap Information, 75 Fed. Reg. 75208 (published 2 December 2010); Real-Time Public Reporting of Swap Transaction Data, 75 Fed. Reg. 76140 (published 7 December 2010); Swap Data Recordkeeping and Reporting Requirements, 75 Fed. Reg. 76574 (published 8 December 2010).

¹⁴ See Consultative Report, 14 (“valuations for many products will differ across institutions, especially for complex derivatives which may not trade on a regular basis.”).

¹⁵ See Confirmation, Portfolio Reconciliation, and Portfolio Compression Requirements for Swap Dealers and Major Swap Participants, 75 Fed. Reg. 81519 (published 28 December 2010).

achieved by computing an average of the submissions that the TR received. We believe that such approach would not result in a loss in quality of the marks that is significant for regulatory purposes.

c. Adjustments

The Consultative Report identified as a potential issue the need to adjust marks because counterparties might store certain information in internal systems.¹⁶ We do not believe that this issue is relevant here, however, because major market participants already frequently produce and communicate internally-calculated marks to their counterparties.

d. Timeliness

The Committees voiced concerns whether counterparty marks could be provided within the required timelines.¹⁷ However, to understand and monitor the risk of their positions, derivative counterparties will need to perform a regular, and often daily, valuation of their positions in any case, either internally or through the use of external third parties. Additionally, counterparty marks are often provided on a daily basis already, and, as mentioned above, this will be even more common as it becomes a regulatory requirement at least in some jurisdictions in the future (e.g., in the US, the DFA and rules proposed by the CFTC and the SEC require the communication of marks on a daily basis).¹⁸ We therefore believe that active market participants should be able to meet the required timelines without significant additional effort.

e. The provision of valuations by TRs would require significant efforts and might not be feasible

For the reasons discussed above, we believe that counterparty marks can effectively address the issues raised by the Committees regarding the calculation of current values for OTC derivatives positions. In contrast, we believe that requiring TRs themselves to produce valuations for all of the positions that they store would create massive operational challenges and would be much more costly for the industry and TRs to implement. Moreover, based on the following considerations, we believe that valuations produced by TRs would produce only inadequate results when compared to the use of counterparty marks:

- TRs do not generally have valuation capabilities for OTC derivatives today and, we believe, it would require significant time and cost for them to build these capabilities even for standard products. Moreover, most TRs will be required to accept *all* swaps in the asset class that they operate in,¹⁹ so they would need to build highly sophisticated modeling capabilities to be able to value even the most complex products.
- TRs would require the reporting of very large and detailed datasets that represent a complete trade description in order to be in a position to produce an independent valuation for complex products. We believe that this would create a significant additional reporting cost for counterparties and for TRs, and will often simply be impossible to achieve.²⁰

¹⁶ See Consultative Report, 14 (“firms may hold pricing/valuation information, or even adjustments, which are not reflected in the inhouse application which would be expected to transmit data to TRs.”).

¹⁷ See *id.* at 14 (“the timely and frequent submission of such data may present significant operational challenges, risks and costs to TRs and participants.”).

¹⁸ See Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 75 Fed. Reg. 80638, 80658-59 (published 22 December 2010) (to be codified at 17 C.F.R. §§ 23.431(a)(c)) (CFTC requiring the provision of a daily mark in certain circumstances); Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 76 Fed. Reg. 42396, 42454 (published 18 July 2011) (to be codified at 17 C.F.R. § 240.15Fh-3(c)) (SEC requiring the provision of a daily mark in certain circumstances).

¹⁹ See Swap Data Repositories: Registration Standards, Duties and Core Principles, 76 Fed. Reg. 54538 (published 1 September 2011).

²⁰ The Committees should note that even the most developed TRs, such as DTCC’s Trade Information Warehouse for credit derivatives, captures only a limited dataset for the more complex products, which does not suffice to perform an actual valuation of these positions.

- If valuations were provided by TRs it would not eliminate the issue of diverging valuations of the same product. This is because several TRs will likely exist in each asset class, each of which is likely to produce a somewhat different valuation for the same product.²¹

We therefore do not believe that it would be practical to require TRs to produce valuations of OTC derivatives for provision to regulators. Instead, the Committees could require TRs to collect counterparty marks and provide them, or a derivation of them, to regulators.

2. Regulators Should Receive Current Market Values from TRs to Ensure That Such Communications Are Performed in a Secure, Auditable, and Efficient Fashion

The Committees noted that current market values could be communicated to regulators: a) directly from the institutions that they supervise; b) via third party providers; or c) via TRs that would collect and store this information centrally for their entire trade population.²²

We believe that regulators should obtain current market values, that are based on counterparty marks, directly from TRs. This will be more efficient than obtaining individual marks from each market participant directly because of the relatively limited number of TRs. Moreover, regulators will probably have established connectivity with TRs already, as opposed to each supervised entity. We further believe that counterparties to OTC derivatives transactions would also prefer this method because it would enable them to make use of established, scalable means to communicate their marks to TRs in an efficient and secure manner.

Comments on Legal Entity Identifiers (“LEIs”)

In the Consultative Report, the Committees also discuss issues related to LEIs, including the appropriate timetable for phased implementation of LEIs and the appropriate governance of the LEI system.²³ We believe that, in this context, regulators should ensure that: (a) the introduction of LEIs builds on global support and their implementation is appropriately phased-in; (b) the operation, governance and compilation of LEIs is inclusive to reflect the views of all stakeholders;²⁴ and (c) several easy-to-use mechanisms to acquire and distribute LEIs are offered.

1. The Introduction Of LEIs Should be Phased-In

Markit supports the LEI initiative and we would welcome its timely and global adoption. However, due to the significant implementation costs of an LEI system, there is a need for broad international support and commitment from all the relevant stakeholders. Further, we believe that the LEI initiative should be phased in with clearly defined milestones. Specifically, regulators should first identify and address any regulatory obstacles to the introduction of LEIs²⁵ and then phase in LEIs by jurisdictions, by the level of detail, and by type of participant:

²¹ Notably, this issue even exists for cleared OTC derivatives in case they are cleared by more than one CCP, as each CCP will determine its daily settlement prices based on its rules and pricing inputs from its clearing members.

²² See Consultative Report, 45 n.96 (“Market values being provided by market participants themselves or incorporated from external third-party pricing sources. In addition, detailed transaction-level data could be used by the TR to generate benchmark valuations internally.”).

²³ See *id.* at 39.

²⁴ For the avoidance of doubt, we do not comment on the proposed LEI core principles of Uniqueness, Neutrality, Reliability, Open Source and Extensibility of the system as we believe they are all logical and well thought-out.

²⁵ Such regulatory obstacles to the implementation of LEIs should be addressed ahead of implementation and as part of ongoing amendments and updates of existing legislation.

a. Phase-in by jurisdiction

Instead of aiming to develop and implement an LEI regime that covers every country in the world from the start, we believe that one should initially focus on the most relevant and/or “easier” jurisdictions. Specifically, the focus of early development should be North America, Europe, and some countries in the Asia-Pacific region because these jurisdictions have highly developed financial markets and supporting infrastructure. However, coverage of other jurisdictions would need to follow based on a clearly articulated, agreed and comprehensive plan for a global roll-out.

b. Phase-in by level of detail

Any initial LEI system may not yet be developed enough to capture each individual trading desk or link all affiliated entities. We therefore believe that regulators must agree early-on as to the prioritisation of the LEI breadth of entity coverage and the granularity of detail that it contains.

c. Phase-in by participant

The implementation costs for a universal LEI system will be significant for many stakeholders, particularly due to necessary changes in IT systems.²⁶ In order to grant entities more time to absorb some of these costs, we believe that the LEI system should be phased-in by type of market participant.

2. All Stakeholders Should Be Involved in the Compilation, Governance and Operation Of LEIs

We support SIFMA’s initial approach in relation to the governance of the LEI system because it includes representatives from most sectors of the industry.²⁷ We believe, however, that any LEI solution provider should actively engage regulatory authorities, industry associations, financial market participants, end-users as well as service providers and data vendors globally on an ongoing basis. Such broad involvement and consultation may be time-intensive but we believe that the ongoing involvement and engagement of all parties is essential to ensure the success of the initiative.

We believe such involvement should be inclusive and not exclude any relevant stakeholders. Therefore, it must extend to all participants that are either direct or indirect users of LEIs.²⁸ Specifically, we believe that representatives of financial institutions, regulatory authorities, industry associations, the buy-side community, as well as service providers and data vendors²⁹ should be asked to participate in the development of universal identifiers.

3. Several Easy To Use Mechanisms To Acquire and Distribute LEIs Should Be Offered

We believe that the LEI system must be universally adopted across jurisdictions, or at least by a critical mass of market participants, in order to be successful. To achieve this goal, we believe that multiple easy-to-use “paths” to receive an LEI should be provided to entities. In this regard, market participants must be able to obtain LEIs both through self-registration and through agent sponsorship. Through a self-registration process, market

²⁶ Given the number and size of systems requiring update within the various impacted organisations, the costs are likely to be unevenly allocated across the industry. Therefore, the large financial institutions, trading/settlement infrastructure and service providers are likely to be required to integrate the LEI within their systems initially in order to facilitate its wider adoption within the industry.

²⁷ See SIFMA, Requirements for a Global Legal Identifier (LEI) Solution, 28 (May 2011), available at <http://www.sifma.org/LEI-Industry-Requirements/>.

²⁸ The Committees requested comment on which parties should be involved in the industry initiative, in order to reach a broad, international industry consensus concerning OTC derivatives product identification and classification in a manner that is fair, balanced, open, and transparent, and considers the interests of all stakeholders.

²⁹ This group should encompass various types of vendors and service providers such as stock exchanges, CCPs, market infrastructure providers such as confirmation platforms, as well as data and news providers.

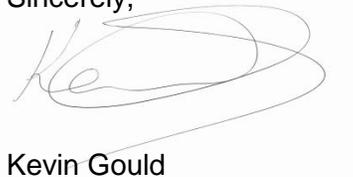
participants should be able to obtain an LEI through a user-friendly website that guides the user step-by-step through the relevant requirements for obtaining an LEI. Through an agent sponsorship process, dealer counterparties should be able to register their counterparties for an LEI as an agent of that counterparty. Agent sponsorship could be performed either on the basis of a bulk counterparty list or via the self-registration website. We believe that both these choices need to be provided because some end-users will not have the time or the resources to obtain an LEI themselves, while other market participants may find it more efficient to obtain an LEI through their counterparty. Furthermore, in addition to functioning as mechanism for LEI applications, a user-friendly website should also be used to disseminate LEIs and their associated source data/documentation.

We believe that the above mechanisms for acquiring and disseminating LEIs should be created early on because this will make the broad usage of the LEI standard more likely.

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We appreciate the opportunity to provide CPSS and IOSCO with our comments in response to their Consultative Report. In the event you may have any questions, please do not hesitate to contact the undersigned or Marcus Schüler at marcus.schueler@markit.com.

Sincerely,



Kevin Gould
President
Markit North America, Inc.