

July 22, 2013

Ms. Elizabeth Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549

Re: ***S7-08-11 / Clearing Agency Standards for Operation and Governance (the “Clearing Agency Proposed Rule”)***<sup>1</sup>

Dear Ms. Murphy:

Markit is pleased to submit the following comments to the Securities and Exchange Commission (the “**Commission**”) regarding the appropriate framework of regulation for “clearing agencies” that solely perform matching, affirmation, confirmation, reconciliation, compression, novation, or substantially similar services (“**independent verification services**” or “**IVS Clearing**”) for transactions in securities and security-based swaps (“**SBS**”).

We are submitting this letter as a follow up to our meetings with Commission Staff regarding the Clearing Agency Proposed Rule, and appreciate the opportunity to continue this dialogue in preparation for the publication of the Final Clearing Agency Standards for clearing agencies that are not traditional central counterparties (“**non-CCPs**”). As detailed below, Markit respectfully requests that the Commission adopt a tailored regulatory framework for clearing agencies performing IVS Clearing modeled after the Commission’s 2001 order exempting Omgeo Matching Services – US, LLC (“**Omgeo**”) from registration as a clearing agency.<sup>2</sup>

## **Introduction**

Markit<sup>3</sup> is a provider of financial information services to the global financial markets, offering independent data, valuations, risk analytics, as well as processing services across regions, asset classes and financial instruments. Our products and services are used by a large number of market participants to reduce risk, increase transparency, and improve the operational efficiency in their financial markets activities.

Most of Markit’s processing services are provided by MarkitSERV,<sup>4</sup> a company that offers confirmation, connectivity, and reporting services to the global OTC derivatives markets, making it easier for participants in these markets to interact with each other. Specifically, MarkitSERV provides trade processing, confirmation, matching, and reconciliation services for OTC derivatives across regions and asset classes, as well as

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<sup>1</sup> Clearing Agency Standards for Operation and Governance, 76 Fed. Reg. 14472 (published March 16, 2011).

<sup>2</sup> See Global Joint Venture Matching Services—US, LLC; Order Granting Exemption from Registration as Clearing Agency, 66 Fed. Reg. 20494 (Apr. 23, 2001) (hereafter, the “**Omgeo Order**”).

<sup>3</sup> Markit is a financial information services company with over 3,000 employees in North America, Europe, and Asia Pacific. The company provides independent data, valuations and processing services for financial products across asset classes in order to reduce risk and improve operational efficiency. Please see [www.markit.com](http://www.markit.com) for additional information.

<sup>4</sup> MarkitSERV, a wholly owned subsidiary of Markit Group Limited, provides a single gateway for OTC derivatives trade processing. The company offers trade processing, confirmation, matching, and reconciliation services across regions and asset classes, including interest rate, credit, equity, and foreign exchange derivatives. MarkitSERV also connects dealers and buy-side institutions to trade execution venues, CCPs, and trade repositories. Please see [www.markitserv.com](http://www.markitserv.com) for additional information.

universal middleware connectivity for downstream processing such as clearing and reporting. Such services, which are offered also by various other providers, are widely used by participants in these markets today and are recognised as tools to increase efficiency, reduce cost, and secure legal certainty. With over 2,500 firms globally using the MarkitSERV platforms, including agents for over 26,000 buy-side fund entities, our legal, operational, and technological infrastructure plays an important role in supporting the OTC derivatives markets in North America, Europe, and the Asia-Pacific region. In 2012, over 20 million OTC derivative transaction processing events were processed using MarkitSERV.

Markit has been actively and constructively engaged in the discussion regarding regulatory reform of financial markets. We regularly provide regulatory authorities with our insights on current market practices, including for example, in relation to the confirmation of derivative transactions, efficient means of reporting transactions to Trade Repositories, clearing connectivity, and portfolio reconciliation practices. We have also advised regulatory bodies on approaches to enable timely and cost-effective implementation of newly established requirements, including for example, the use of a multi-layered phase-in or by providing participants with a choice of means for satisfying regulatory requirements. Over the last several years, we have submitted more than 80 comment letters to regulatory authorities around the world, and participated in numerous roundtable discussions.

## **Executive Summary**

As the Commission has noted,<sup>5</sup> the Securities Exchange Act of 1934 (the “**Exchange Act**”) defines the term “clearing agency” broadly to include, in addition to providers of traditional CCP clearing services, entities that operate “facilities for the comparison of data respecting the terms of settlement of securities transactions.”<sup>6</sup> The Commission has proposed to interpret this provision to require providers of certain “matching” services, but not other forms of data verification, to register as clearing agencies.<sup>7</sup> MarkitSERV filed a comment letter in response to this proposal on April 29, 2011 (the “**MarkitSERV Comment Letter**”),<sup>8</sup> where we requested that, among other things, the category of non-CCP clearing agencies (including those performing IVS Clearing) be appropriately defined and that the compliance obligations applicable to such clearing agencies be proportionate to the functions they perform.

The Commission has stated that it “preliminarily agrees with commenters that it is appropriate to consider a tailored framework of regulation for clearing agencies that perform certain post-trade processing services because such activities do not involve the same credit, market and operational risk concerns that are presented by traditional CCP clearing agencies.”<sup>9</sup> Markit appreciates this consideration and would urge the Commission to adopt a tailored regulatory framework with the following attributes for IVS Clearing providers:

- **Tailored compliance obligations.** In the Omgeo Order, the Commission granted an exemption from registration to Omgeo, permitting Omgeo to provide specified electronic confirmation and central matching services,<sup>10</sup> subject to Omgeo’s compliance with certain obligations relating to,

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<sup>5</sup> See Clearing Agency Standards, Final Rule, 77 Fed. Reg. 66220, 66228 (Nov. 2, 2012); see also Securities Exchange Act of 1934 § 3(a)(23)(A).

<sup>6</sup> Securities Exchange Act, § 3(a)(23)(A), 15 U.S.C. § 78c(a)(23). Note that the statutory language makes no distinction between matching and affirmation services, nor does it reference any degree of legal certainty that must result from this “comparison of data” in order for an entity to fall into the definition of a Clearing Agency.

<sup>7</sup> Clearing Agency Proposed Rule, 76 Fed. Reg. 14472, 14495

<sup>8</sup> See Letter from MarkitSERV to the SEC (April 29, 2011), [available here](#); see also Letter from MarkitSERV to the CFTC (June 3, 2011), [available here](#).

<sup>9</sup> See 77 Fed. Reg. 66220, 66228.

<sup>10</sup> Omgeo’s confirmation service would “transmit messages (*i.e.*, confirmation and affirmation messages) among broker-dealers, institutional customers, and custodian banks and would ultimately result in the production of an affirmed trade confirmation.” Omgeo Order, 66 Fed. Reg. at 20496. Omgeo’s matching service would “compare or match trade information submitted by a broker-dealer (*i.e.*,

among other things, operations, information sharing and recordkeeping (the “**Omgeo Standards**”).<sup>11</sup> MarkitSERV provides the same type of confirmation and matching services for, among other types of products, security-based swaps. Markit therefore believes that the Commission’s requirements outlined in the Omgeo Standards provide the appropriate level of oversight and control over IVS Clearing and, thus, should serve as a framework for any rules governing such clearing agencies. The following table summarizes these standards that Markit believes should be applied to IVS Clearing versus the standards that would apply under the Clearing Agency Proposed Rule.

	<b>Markit Proposal</b>	<b>SEC Proposal</b>
Services Covered	<p>All IVS Clearing providers should be covered by non-CCP clearing agency regulations, including providers of:</p> <ul style="list-style-type: none"> <li>• Matching</li> <li>• Affirmation</li> <li>• Confirmation</li> <li>• Reconciliation</li> <li>• Substantially similar services</li> </ul>	<p>Providers of the following services are covered by non-CCP clearing agency regulations:</p> <ul style="list-style-type: none"> <li>• Matching</li> <li>• Compression</li> <li>• Tear-up</li> <li>• Collateral management services</li> </ul>
Operational Requirements	<ul style="list-style-type: none"> <li>• Pre-operation audit report</li> <li>• Annual audit reports</li> <li>• System outage reports</li> <li>• Notification of system changes</li> <li>• Requests from the Commission</li> <li>• Periodic reports</li> <li>• Recordkeeping</li> <li>• Provision of service agreements to the Commission</li> </ul>	<ul style="list-style-type: none"> <li>• Audited financial statements</li> <li>• Transparent and enforceable rules</li> <li>• Participation requirements</li> <li>• Custody of assets and investment risk</li> <li>• Identification/mitigation of operational risk</li> <li>• Money settlement risks</li> <li>• Cost-effectiveness</li> <li>• Links</li> <li>• Governance</li> <li>• Information on services</li> <li>• Default procedures</li> <li>• Protection of confidential information</li> <li>• Conflicts of interest</li> </ul>

confirmation information) with the trade information submitted by an institutional customer (i.e., allocation instructions) to produce an affirmed confirmation.” *Id.*

<sup>11</sup> See Omgeo Order, 66 Fed. Reg. at 20495 (“This order grants [Omgeo] an exemption from registration as a clearing agency subject to certain conditions and limitations described below in order that GJVMS may offer an electronic trade confirmation (“**ETC**”) service and a Central Matching Service.”).

		<ul style="list-style-type: none"><li>• Standards for board of directors and committees</li><li>• Chief compliance officer</li></ul>
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- **Fair competition among IVS Clearing providers.** In the Clearing Agency Proposed Rule, the Commission stated that it preliminarily believed that entities providing matching services would meet the definition of a “clearing agency,” but that providers of certain affirmation and novation services would generally not fall within this definition.<sup>12</sup> As described below, we believe that all IVS Clearing providers fall within the statutory definition of a clearing agency because they provide facilities for the comparison of data,<sup>13</sup> and should therefore be regulated similarly. Moreover, the difference between matching and affirmation providers is a distinction without a difference, so the Commission should ensure that equivalent and competing service providers are exposed to comparable registration and regulatory requirements by requiring all IVS providers to register as non-CCP clearing agencies.

## **Comments**

### **A. The Omgeo Standards Provide an Appropriate Framework for Entities Providing IVS Clearing Services**

We agree with the Commission’s preliminary view that non-CCPs should be subject to a tailored compliance regime, rather than the full regime applicable to CCP clearing agencies, because the activities engaged in by non-CCPs “do not involve the same credit, market and operational risk concerns that are presented by” CCP clearing agencies.<sup>14</sup> For example, issues related to conflicts of interest and access have little relevance to non-CCP clearing agencies because market participants utilizing IVS Clearing services have an incentive to encourage industry-wide participation in those services. The implementation of electronic confirmation of swaps, for example, is based on an industry collaborative process that is open to all market participants. We also believe there is little utility in requiring non-CCP clearing agencies to comply with requirements related to, but not limited to: (i) custody of assets and investment risks in rule 17Ad-22(d)(3); (ii) money settlement risks in rule 17Ad-22(d)(5); (iii) default procedures in rule 17Ad- 22(d)(11); and (iv) many of the requirements related to chief compliance officers in rule 3Cj-1 because these issues are not relevant in the context of IVS Clearing.

In the Omgeo Order and its progeny,<sup>15</sup> the Commission adopted a reasoned approach to the regulation of a non-CCP clearing agency, which has remained relevant for over a decade. The Commission stated in the Omgeo Order that because the matching service would be the only clearing agency function performed by Omgeo, an exemption from full registration as a clearing agency was appropriate.<sup>16</sup> MarkitSERV and other matching service providers offer the same type of matching services as Omgeo for, among other types of products, security-based swaps. Accordingly, we believe that relief from full clearing agency registration would be appropriate and that the Omgeo Standards (with appropriate modifications to account for technological developments over the intervening period) represent the sort of tailored regime envisioned by the Commission and would provide the proper framework for IVS Clearing providers. The Commission could accomplish this by

<sup>12</sup> See Clearing Agency Proposed Rule, 76 Fed. Reg. at 14495.

<sup>13</sup> See Securities Exchange Act, § 3(a)(23)(A), 15 U.S.C. § 78c(a)(23) (“The term “clearing agency” means any person who . . . provides facilities for comparison of data respecting the terms of settlement of securities transactions. . . .”).

<sup>14</sup> See Clearing Agency Proposed Rule, 76 Fed. Reg. at 14495.

<sup>15</sup> See e.g., Thomson Financial Technology Services, Inc.; Order Approving Application for Exemption From Registration as a Clearing Agency (Exchange Act Release No. 34-41377), 64 Fed. Reg. 25948 (May 13, 1999) (hereinafter, the “**Thomson Order**”).

<sup>16</sup> See Omgeo Order, 66 Fed. Reg. at 20498.

limiting the requirements applicable to IVS Clearing providers through the rulemaking process or by granting exemptive relief for non-CCP clearing agencies in line with the Omgeo Standards.<sup>17</sup>

We note that one area of the Omgeo Order, which imposed several conditions related to interoperability, is inapposite in the IVS Clearing context. These conditions were imposed at least in part because of the unique circumstances of Omgeo combining “the two principal systems used by broker-dealers and institutional investors for post-trade, pre-settlement processing of U.S. trades.”<sup>18</sup> However, such competitive concerns are not present here, as there is no such combination contemplated in the industry to our knowledge and, as we have discussed with Commission Staff, there are many IVS Clearing providers.

We therefore do not believe that interoperability conditions need be imposed on IVS Clearing providers generally, because they are not necessary to achieve the goals of the Commission’s tailored Omgeo Standards; namely: “to monitor [Omgeo]’s risk management procedures, operational capacity and safeguards, corporate structure, and ability to operate in a manner to further the fundamental goals of section 17A.”<sup>19</sup> Indeed, when the Commission granted an exemption from clearing agency registration requirements to Thomson Financial Technology Services, Inc. in relation to its matching services, the Commission did not impose these interoperability requirements.<sup>20</sup> We therefore urge the Commission to impose only the operational requirements from the Omgeo Standards on IVS Clearing providers.

## **B. Registration and Regulation of IVS Clearing Providers Should be Applied Uniformly**

We believe that the non-CCP compliance regime described above should apply to all IVS Clearing providers—not merely providers of matching services whose activities result in creating legally binding contracts—in order to ensure that the regulatory structure applicable to these entities is equitable (ensuring a level-playing field between competing providers), does not leave any regulatory gaps and does not promote possible regulatory arbitrage. In order to better explain the similarities and differences between the various types of IVS Clearing services and why it is important that these services all be regulated under one uniform set of standards, we will briefly describe how SBS transactions are currently confirmed (as explained in greater detail in the MarkitSERV Comment Letter<sup>21</sup>).

### **(i) Background on Independent Verification Services**

Counterparties to a swap or SBS typically use one of two methods to agree that the fully enriched set of transaction details accurately reflects the intent of the parties:

(a) *Affirmation*: In the affirmation method, one party alleges the details of the swap transaction to their counterparty. The counterparty will then check or compare these details and, if appropriate, affirm that they are correct. For transactions that are facilitated through an intermediary, e.g. an inter-dealer broker or an electronic trading system, the intermediary may propose the transaction details to both parties, who then each compare and affirm them. Certain affirmation service providers will not produce a legally binding contract. Instead, the service provider merely sends the details of a transaction to both counterparties, who compare those details against their own. The service provider then sends the transaction to a CCP, which creates a legally binding contract.

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<sup>17</sup> See Omgeo Order, 66 Fed. Reg. at 20498; Self-Regulatory Organizations; Thomson Order, 64 Fed. Reg. 25948, 25949.

<sup>18</sup> See Omgeo Order, 66 Fed. Reg. at 20495.

<sup>19</sup> See Omgeo Order, 68 Fed. Reg. at 20501.

<sup>20</sup> See Thomson Order, 64 Fed. Reg. at 25950.

<sup>21</sup> See Letter from MarkitSERV to the SEC (April 29, 2011), [available here](#).

(b) *Matching*: As part of the matching method, both counterparties to the transaction allege the transaction details to each other, which are then compared. The comparison can be performed in a centralized fashion, *i.e.*, “central matching” through electronic matching services such as those provided by MarkitSERV. It can also be performed in a localized manner, where one or both counterparties make their own comparison and notify the other party of any discrepancies. MarkitSERV creates a legally binding contract through its matching service.

Affirmation and local matching can also be used together, where the parties who receive alleged details of the swap transaction will perform a local match to their satisfaction, and then affirm to their counterparty.

**(ii) All IVS Clearing Providers Should be Comparably Regulated**

**Matching and Affirmation Are Comparable Procedures**

The Clearing Agency Proposed Rule would require providers of certain “matching” services, but not other forms of data verification, to register as clearing agencies.<sup>22</sup> We support the requirement for matching service providers to register and comply with appropriately tailored regulations, but believe that the same obligations should apply to all IVS Clearing providers. As described above, trade affirmation and matching are nothing but two alternative techniques that lead to the same result—namely, enabling the counterparties to an SBS to compare their data and reach an agreement on the complete set of transaction details in an efficient and timely manner with the providers of these services performing an “independent verification.” Moreover, matching and affirmation service providers often compete with each other. We therefore believe that requiring one type of verification provider, but not others, to register would constrain competition, create a regulatory loophole and invite regulatory arbitrage.

Affirmation and matching are both used extensively for the efficient, automated comparison and verification of SBS and swap transactions. MarkitSERV facilitates confirmation of SBS and swap transactions in several asset classes through various techniques, including affirmation, matching, and affirmation with local matching. Each of these methods is widely used by a variety of market participant types. Quarterly metrics show that 99% of the relevant credit derivative transactions were electronically confirmed, mostly using a central matching method. In equity derivatives, 40% of the transactions were electronically confirmed using a mixture of central matching, affirmation and affirmation with local matching. Of the relevant interest rate derivative transactions 85% were electronically confirmed, largely using affirmation or affirmation with local matching.

While affirmation is the prevalent method in some asset classes, matching dominates in others, and a variety of techniques are used in the remainder. To some extent, the prevalence of one method versus the other in a given asset class is driven by practicalities. Matching is generally performed by submitting transactions—which have already been captured in a trade booking system—to a matching service provider. In contrast, transactions are typically submitted for affirmation by an execution venue (such as an inter-dealer broker) and simultaneously routed to a counterparty’s trade capture system.

Ultimately, these are simply different routes to the same desired result. Accordingly, we do not believe that the practical differences between affirmation and matching warrant the regulation of one form of verification but not the other.

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<sup>22</sup> See Clearing Agency Proposed Rule, 76 Fed. Reg. at 14495.

### All IVS Clearing Providers Should be Comparably Regulated

The Proposed Rule would only require IVS Clearing providers to register as a non-CCP clearing agency if their activity results in the issuance of a legally binding contract, while those who only perform “preliminary comparisons” would be left unregistered.<sup>23</sup> We believe that this approach would be counter-productive for a number of reasons:

- First, both types of providers fall within the statutory definition of a clearing agency. A clearing agency is any person that provides facilities for comparison of data respecting the terms of settlement of securities transactions.<sup>24</sup> While the Commission has stated that it preliminarily believed that “preliminary comparisons” would not trigger registration requirements,<sup>25</sup> we do not believe this understanding accurately reflects the function of these providers in the marketplace. As described above, affirmation providers provide the ability (typically through some form of electronic functionality; *i.e.*, a “facility”) that either sends data to both counterparties or allows those counterparties to allege SB swap terms to one another in order to compare that data against their own. Thus affirmation providers provide “facilities for the comparison of data” and should register as clearing agencies in the same manner as other IVS Clearing providers.
- Second, such approach may unintentionally benefit providers that do not provide legal certainty while disadvantaging those that do provide legal certainty. This gap in regulation could lead to regulatory arbitrage that is at odds with Congressional intent to reduce risk in the swaps markets.
- Third, all IVS Clearing providers are critical to the routing of SB swaps and should be subject to some form of regulation in keeping with Congressional intent. IVS Clearing providers generate a definitive record of a transaction that is used for subsequent processing, and IVS Clearing providers are typically responsible for communicating transaction data to a wide array of market participants, including execution venues, counterparties, CCPs, and SDRs. Their proper functioning is therefore critical to mitigating risk and ensuring that the SB swaps market functions seamlessly.
- Fourth, regulating only providers whose activities result in legally binding contracts but not others would result in an unnecessary restraint on competition because these entities directly compete with each other. A registration requirement that favors one group of service providers over the other should be avoided.

We therefore believe that any registration and compliance obligations applicable to non-CCP clearing agencies should be applicable to all IVS Clearing providers. The Commission appeared to agree when it issued an order temporarily exempting non-CCP clearing agencies from registration requirements and applied that exemption to, among other persons, matching service providers and providers of “substantially similar services.”<sup>26</sup> We urge the Commission to clarify that the non-CCP clearing agency regulations apply to all IVS Clearing providers, which could be defined as:

*Entities that act independently from, but on behalf of, all counterparties to a SBS to facilitate the agreement between those counterparties upon a verified record of SBS transaction details where such record is relied upon by the counterparties to the SBS and other market participants*

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<sup>23</sup> Matching which results in the “issuance of legally binding matched terms” vs “perform preliminary comparisons”.

<sup>24</sup> See Securities Exchange Act, § 3(a)(23)(A), 15 U.S.C. § 78c(a)(23).

<sup>25</sup> See Clearing Agency Proposed Rule, 76 Fed. Reg. at 14495.

<sup>26</sup> See Order Pursuant to Section 36 of the Securities Exchange Act of 1934 Granting Temporary Exemptions from Clearing Agency Registration Requirements under Section 17A(b) of the Exchange Act for Entities Providing Certain Clearing Services for Security-Based Swaps, Release No. 34-34796 at 8, 12.

*for communication of transaction details to a CCP Clearing Agency or security-based swap data repository.<sup>27</sup>*

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Markit appreciates the opportunity to comment on the appropriate framework of regulation for clearing agencies performing IVS, including affirmation, matching, or substantially similar services for SBS transaction, and and would be happy to elaborate or further discuss any of the points raised. In the event you may have any questions, please do not hesitate to contact the undersigned or Marcus Schüler at [marcus.schueler@markit.com](mailto:marcus.schueler@markit.com).

Yours sincerely,



Jeff Gooch  
Head of Processing  
Markit

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<sup>27</sup> See the MarkitSERV Comment Letter. Note that our definition of independent verification service providers in the MarkitSERV Comment Letter was limited to entities that facilitate the agreement of a verified record of *the complete* transaction details. In order to ensure that entities do not evade regulation by facilitating agreement on some but not all of the transaction details, we have modified that definition in this letter. We have also modified the definition in an attempt to clarify the reach of the term “independent verification service providers.”