

Mr David Stawick,
Secretary
Commodity Futures and Trading Commission
Three Lafayette Centre, 1155 21st Street, N.W
Washington, DC 20581

Re: RIN 3038-AD08 - Notice of Proposed Rulemaking on Real Time Public Reporting of Swap Transaction Data

Dear Mr Stawick,

TriOptima welcomes the opportunity to submit comments in response to the proposed rules on Real Time Public Reporting of Swap Transaction Data in which the Commodity Futures Trading Commission (“the Commission”) solicited comments on its proposed rules to implement Section VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”, and such rules, the “Proposed Rules”).

TriOptima’s comments reflect our extensive experience serving as a key provider of OTC derivatives market infrastructure offering operational and counterparty credit risk management tools to the OTC derivatives market. TriOptima has significantly contributed to the promotion of better and safer OTC markets including:

- Terminating interest rate swap derivatives in 23 currencies with a notional principal value of \$108 trillion , with the participation of more than 150 dealing institutions globally over the course of the past ten years;
- Terminating and compressing more than \$ 68.2 trillion in notional value of credit derivatives since 2005, eliminating 50% of the global gross notional outstanding in 2008 alone;
- Maintaining extensive data for more than 6 million live OTC derivatives contracts covering all asset class (interest rates, credit, commodity, FX, equity, etc.) from more than 2,750 legal entities, representing approximately 75% of all non-cleared OTC derivatives, for the purpose of reconciling and ensuring the accuracy of that data;
- Developing and supporting the global Interest Rates Trade Reporting Repository (“the Rates Repository”) which produces weekly reports covering 3.9 million OTC interest rate derivative transactions with a notional value of \$486 trillion for regulatory review.

We would like to start by making two general observations on the nature of the OTC derivatives market which we believe are important to take into account in the rule making process.

The first observation is that “OTC derivatives” is a label that encompasses a wide variety of different types of financial contracts. At one end of the spectrum there are financial contracts that are so mature and popular that they have reached a fairly high level of standardization, which has facilitated the implementation of infrastructure to support a number of processing needs like electronic execution, confirmation, allocation, settlements, collateralization etc. At the other end of the spectrum there are bespoke transactions, customized to the individual needs of clients, where the degree of standardization and infrastructure support is low, and the rate of innovation is high. The low volumes traded in these bespoke products and their customized nature makes investment in automation prohibitively expensive.

When it comes to real time price dissemination, both the transparency benefits as well as the challenges in implementation are vastly different at the two ends of the spectrum.

The second observation is that OTC derivatives markets are truly global with counterparties from all over the world trading with each other. US regulated entities constitute a varying proportion of the total number of participants in various geographical markets of OTC derivatives. For markets where US-based entities only make up a small fraction of the total number of participants (e.g., some Asian markets), the proposed rules will create problems. US-based entities could potentially find themselves at a competitive disadvantage. Moreover, the rules for determining block trade sizes will be difficult to implement in these markets since only a small fraction of the total market is available for the determination.

Reportable swap transactions

In the definition of reportable swap transactions, the necessary criteria should stipulate that it relates to arms-length transactions between two independent parties, and that such transactions should result in a corresponding change in the market risk position for the two parties.

The purpose of having such criteria is to exclude portfolio management transactions which are undertaken for the purpose of managing credit risk or operational risk and/or cost and which do not change the risk position of the parties.

Such portfolio management transactions could for example be bilateral or multilateral portfolio compression exercises involving both the termination of existing swaps and possibly the creation of new replacement swaps, but where the compression package as a whole is market risk neutral. A market risk neutral package of transactions means that the parties have bought as much as they have sold, or terminated as many long positions as short positions. The market risk neutrality means that the price of the individual transactions in the package is irrelevant and thus it has no price discovery value for other parties or the public.

The criteria would also need to exclude internal transactions between related or affiliated parties such as back-to-back transactions between trading centers for the purpose of transferring the management of risk, where the pricing of the individual transaction could be influenced by group internal issues.

Categorization of swaps

In the Proposed Rules, the Commission has noted the requirement for a categorization of swaps when it relates to the determination of appropriate block trade sizes.

Several institutions, including banks, software firms and academics, have spent considerable time thinking about how to categorize or define OTC derivatives. Such categorization has proven to be elusive.

The reason for this is that an OTC derivative contract essentially is a collection of financial elements, where a financial element is some type of fixed or contingent flow of financial assets. . The choice of elements collected is driven by the users' desire to take or mitigate risks, and not necessarily any relationship between the elements. Innovation in OTC derivatives is mainly done by compiling a new collection of financial elements or inventing a new contingency, possibly referencing some new underlying source of risk.

Some of these collections have achieved a high degree of popularity and therefore been given their own names like "Interest Rate Swap", "Forward Rate Agreement", "Total Return Swap" or "Variance Swap", and a certain degree of standardization has evolved around trading and post trade processing.

It should be noted that these names are simply labels, attached primarily for convenience. There are no stringent definitions of these names, and they cannot be the basis for any categorization.

The potential variation in the construction of an OTC derivative means that regardless of categorization there will always be contracts that don't fit, and rules need to be articulated on how these contracts should be handled.

Data standards for reporting and dissemination

A significant portion of OTC derivative transactions are unique, i.e. the exact same contract will in most cases never be traded again. (There are some exceptions to this rule, for example certain types of credit derivatives have been standardized to a large extent and contracts with the same details are traded by multiple counterparties).

The uniqueness of some OTC derivatives means that the price of an executed transaction cannot be used directly for comparison purposes. Instead, institutions that trade in such unique contracts use external price information in well-defined and more frequently traded instruments as benchmarks for calibrating valuation models' inputs like yield curves, volatility surfaces, correlations etc. Only after

using such prices to recalibrate such valuation model inputs, can a comparison then be made on a similar but not identical contract.

For more complex instruments that depend on two or more valuation models' inputs, (for example options that depend on both the underlying value, as well as the volatility of that value) a single price on a particular contract is not sufficient to recalibrate all valuation model inputs. On the contrary, this would require simultaneous and independent price information on several contracts, possibly of different types, in order to do the recalibration.

There are indeed parts of the OTC derivatives markets that are liquid enough to provide simultaneous independent price information for multi-parameter contracts, (possibly USD interest rates swaps and swaptions), but there are also parts of the OTC derivatives markets where the contracts are either bespoke, complex or illiquid; and the information is not available. The transparency value in disseminating prices to the public and other market participants on such contracts is therefore very small. Furthermore, the technical issues in setting up a real-time price dissemination function for such bespoke, complex or illiquid contracts are vastly more complex than for the relatively standardized and more frequently traded OTC derivatives.

The usefulness of real-time prices on executed transactions is directly linked to the receiving party's ability to interpret both the contract details, as well as the price, programmatically. In order for institutions and software firms to make the necessary adaptations of their systems to do that, they would require detailed specifications of all types of contracts and prices that might exist. Furthermore, the SDR or the real-time price disseminator would also need to follow the same detailed specifications.

To accomplish the goal of the Proposed Rule, the regulations on real-time price reporting need to stipulate a detailed data standard for how contracts and prices should be represented, so that it can be accurately implemented by both the recipients, as well as the disseminators, of real-time price information. Changes may be made to the standards over time, but the introduction of such changes must allow market participants sufficient time to make the necessary adaptations to their systems.

The data standard should of course be as inclusive as possible, but any data standards for OTC derivatives will never cover 100% of all possible contracts as long as parties have the freedom to bilaterally negotiate customized OTC derivative contracts to meet the bespoke and precise hedging needs of the end users. From a market transparency perspective, this lack of completeness is not a significant problem, since the transparency value of such bespoke contracts is very low.

Determination of block trade size

The purpose of having specific rules for "block trades" is that such trades would have a significant price impact if they had to be traded on a regulated market, and hence they are allowed to be traded bilaterally. Another reason is that having to report a large notional swap in real-time would increase the market-maker's

cost of hedging such a trade. This would make market-makers less willing to take on such a transaction and thus would reduce liquidity in the market and/or increase the bid-offer spread, both to the detriment of end-users.

The NPR states: *“In developing the proposed rules with respect to block trades and large notional swaps, the Commission considered its guidance with respect to block trades in the futures markets. Additionally, the Commission considered the treatment of block trades in other markets (both foreign and domestic), such as those for equities, options and corporate bonds.”*

We would like to point out that, based on an analysis we performed on the data in the Rates Repository, the turnover (measured in terms of the number of individual transactions traded in a certain time span) is orders of magnitude smaller in the OTC derivatives market than in the other markets the Commission has considered.

In analysing the data in the global Interest Rate Trade Reporting Repository, we found that the average number of interest rate swap trades was 3,600 per day in the month of June 2010. This represents trades where at least one of the parties is a G14 bank, which is the case for the distinct majority of trading volume and is likely to continue to be so in the future. This trade count is the aggregate across all variations of IR swaps, all maturities and all currencies, of which the biggest are USD with 1,200 trades per day and EUR with 830 trades per day.

Breaking down the numbers by maturities we found that approximately half of the new trades are either forward starting swaps, or ones maturing on “odd” end dates, and that the other half has “standard” full year maturities. The most liquid full-year IRS swap contract was the 10 year USD swap where 208 trades were done on average each day. This trade count should then be broken down on different indices, and rolling periods etc. in order to establish the trade count for swaps where it may make sense to compare prices.

Most of the “standardized” swaps in other maturities and currencies trade less than 20 contracts per day, which makes it prohibitively difficult to establish a meaningful price comparison between two transactions. Furthermore, a “standardized” full-year contract traded today will have a different end date compared to a “standardized” full year contract traded yesterday, which makes price comparisons between trading days difficult as well.

We believe that the turnover of a market must be factored in when determining block trade sizes and in particular the appropriate time delay for public dissemination of such block transaction. In an extreme but possible example, there could be a part of the OTC market that on average transacts one 50 million contract per day. The Proposed Rules would then result in a block size of 250 million which represents 5 days of turnover. A 15 minute time delay in the reporting of such a transaction seems insufficient.

Furthermore, we would like to see some guidance on how the block trading size should be determined in other geographical markets where US-regulated entities represent only a small fraction of the total market (e.g. interest rate swaps in various Asian currencies).

We appreciate the ability to provide our comments on the Proposed Rules and look forward to working with the Commission as you continue the rulemaking process. Please feel free to contact us at your convenience with any questions.

Sincerely,

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