

October 14, 2019

VIA ELECTRONIC SUBMISSION

Mr. Christopher J. Kirkpatrick
Secretary of the Commission
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Comments on the Proposed Rule, *Certain Swap Data Repository and Data Reporting Requirements* (RIN 3038-AE32)

Dear Mr. Kirkpatrick:

I. INTRODUCTION

On behalf of The Commercial Energy Working Group (the "**Working Group**"), Eversheds Sutherland (US) LLP submits this letter in response to the request for public comment set forth in the U.S. Commodity Futures Trading Commission's (the "**CFTC**" or "**Commission**") Proposed Rule, *Certain Swap Data Repository and Data Reporting Requirements* (the "**Proposed Rule**").¹

The Working Group is a diverse group of commercial firms in the energy industry whose primary business activity is the physical delivery of one or more energy commodities to others, including industrial, commercial, and residential consumers. Members of the Working Group are producers, processors, merchandisers, and owners of energy commodities. Among the members of the Working Group are some of the largest users of energy derivatives in the United States and globally. The Working Group considers and responds to requests for comment regarding regulatory and legislative developments with respect to the trading of energy commodities, including derivatives and other contracts that reference energy commodities.

II. COMMENTS OF THE WORKING GROUP

The Working Group appreciates the Commission's ongoing efforts to streamline and improve the swap data reporting paradigm set out in Parts 43, 45, and 49 of the CFTC's regulations. Among other things, accurate and timely swap data will allow the Commission to better understand and protect the U.S. swap markets. However, necessary improvements

¹ See Proposed Rule, *Certain Swap Data Repository and Data Reporting Requirements*, 84 Fed. Reg. 21,044 (May 13, 2019), <https://www.cftc.gov/sites/default/files/2019/05/2019-08788a.pdf>.

to the swap reporting paradigm should be made in a targeted manner that first identifies the root causes of data and reporting issues and then addresses those root causes in the most efficient and effective manner possible.

The Working Group is concerned that certain of the Proposed Rule's proposals designed to improve data quality may not have the effect the Commission anticipates while simultaneously imposing material burdens on reporting counterparties, potentially resulting in liquidity implications for energy derivatives markets. As discussed further below, the Working Group believes that the Commission might be able to more fully address its data quality concerns while limiting the impact on reporting counterparties through more targeted changes to its swap data reporting paradigm.

A. The Proposed Rule's Verification Process Does Not Address the Main Drivers of Swap Data Quality Issues.

As noted above, the Working Group understands and supports the Commission's desire for accurate and timely swap data, and generally supports the goal of addressing the shortcomings of the CFTC's swap data reporting paradigm. However, the Proposed Rule does not make clear what those shortcomings are, and more importantly, does not clearly identify the root causes of those shortcomings.

In the preamble text of the Proposed Rule, the identification of issues and their causes is limited to statements like:

in the processing of swap data to generate the CFTC's Weekly Swaps Report, for example, there are instances when the notional amount differs between the Commission's open swaps information and the swap data reported for the same swap. Other common examples of discrepancies include incorrect references to an underlying currency, such as a notional value incorrectly linked to U.S. dollars instead of Japanese Yen.²

In the Working Group's experience, these types of errors, as well as most other common types of reporting errors, are largely caused by at least one of three issues: (i) shortcomings with respect to the data submission and acceptance process at the swap data repository ("**SDR**"); (ii) a lack of clarity with respect to the format of a data element; or (iii) errors in the trade entry process.

As discussed further below, the Proposed Rule and its verification process, in particular, likely would not adequately address these sources of errors. Not only would the proposed verification process likely not be effective, it could also impose material costs on non-swap dealer reporting counterparties who, because of the lower volume of trades that they report, utilize a more manual reporting process. Put another way, if certain reporting counterparties will be required to verify in a short period of time each line of reported data on a monthly basis, then the additional work-hours needed to be a reporting counterparty may cause smaller reporting counterparties to cease acting as such. A reduction in the number of such small reporting counterparties could have the consequence of limiting the availability of counterparties in commodity derivatives markets.³

² Proposed Rule at 21,081.

³ Based on the information provided by Commissioner Stump in her concurrence, approximately 15% of commodity derivatives trades are reported by non-swap dealers. See *Statement of Concurrence of Commissioner Dawn D. Stump on Proposed Rule Amendments to the Commission's Regulations Relating to Certain Swap Data Repository and Data Reporting Requirements* (Apr. 25, 2019),

1. *The Proposed Rule Does Not Directly Address SDR-Related Reporting Errors*

With respect to SDR-related issues, in the experience of the Working Group, where an SDR has a very well-defined set of requirements with respect to how each data element is reported to the SDR, issues like the notional amount problem noted by the Commission can be prevented. Put differently, if an SDR rejects swap reports where a data field does not meet clear, rigid formatting requirements, many reporting format errors are addressed before they enter the reporting eco-system. Accordingly, this type of issue or error would be best addressed by imposing obligations on SDRs to implement and enforce clear and rigid requirements for swap data reported to them. Further, the CFTC should also require consistency across SDRs as to how each data field must be treated and formatted.

The Proposed Rule's data verification process would likely not address the type of errors discussed above. Specifically, unless an SDR, at a later date, identifies the reporting formatting errors, asking a reporting counterparty that is not aware of an issue to confirm that the data they reported is accurate will do little to actually rectify errors. If the SDR is able to identify the formatting errors at a later date, it should also be able to do so prior to submission and should be able to prevent submission of improperly formatted data, again limiting the value of the proposed verification process.

2. *The Proposed Rule Does Not Directly Address Reporting Errors Based on Differing Interpretations of What Must Be Reported for Particular Data Fields*

Another potential source of reporting data quality issues is likely an absence of clarity at the reporting counterparty and SDR levels as to the requirements of particular data fields. This absence of clarity can obviously result in errors and data inconsistency. Like the SDR-related issues discussed above, this would be best addressed through improved guidance from the CFTC to both reporting counterparties and SDRs rather than the proposed verification process.

3. *The Proposed Rule Does Not Directly Address Reporting Errors From Faulty Deal Entry*

In the Working Group's experience, another source of reporting errors can be traced back to errors made when entering trades into a counterparty's trade capture system. Such errors are an inevitable feature of a manual deal entry process, and market participants typically have a number of overlapping internal control mechanisms designed to catch such errors prior to the data related to those transactions being reported to an SDR. Such internal control mechanisms include trade reconciliations and the use of electronic trade confirmation systems like eConfirm.

It is important to note that these internal control mechanisms would exist independent of any regulatory obligation to report swap data to SDRs as the accuracy of transaction-level information is key to a market participant's ability to manage, among other things, market risk, credit risk, and trade settlement. Further, in practice, registered swap dealers likely

<https://cftc.gov/PressRoom/SpeechesTestimony/stumpstatement042519>. If such entities do not act as reporting counterparties, then a material source of liquidity in commodity derivatives markets would disappear.

have such mechanisms in place to comply with their recordkeeping and risk management obligations under Part 23 of the CFTC's regulations.

In the event that a trade entry error results in an inaccurate report to an SDR, it is unlikely that the Proposed Rule's verification process would discover that error. As with the other types of errors discussed above, verifying the reporting counterparty's records against the data they reported is not likely to uncover an error made prior to the data being reported. It is much more likely that a counterparty's internal control mechanisms designed to review the data in a trade capture system would discover the error and the reporting counterparty would then have to correct the error independent of the proposed verification process.

4. *To Better Address the Source of Data Reporting Issues the CFTC Should Focus on Applying Uniform Standards and Guidance on SDRs*

As noted above, in the Working Group's experience, the most likely root causes of the majority of the Commission's swap data issues would not be effectively addressed through the Proposed Rule's verification process. As such, the Working Group respectfully suggests that the Commission focus its efforts on:

- (i) ensuring that SDRs have clear and rigorous standards in place to prevent inaccurate data from entering the SDR in the first place;
- (ii) improving the consistency across SDRs with respect to the format in which data is received;
- (iii) providing more defined guidance to SDRs and reporting counterparties with respect to problem data fields; and
- (iv) emphasizing swap dealer compliance with aspects of Part 23 that feed into the swap data reporting process.⁴

Taken together, these four suggestions likely would have a greater impact in furtherance of the Commission's swap data accuracy initiatives than the proposed verification process and likely would impose a lesser burden on market participants than the proposed verification process.

Further, the Commission could easily address suggestion (i) in a manner that satisfies the SDR's statutory obligation to confirm the accuracy of submitted data prior to submission rather than adopting the proposed after-the-fact verification process. In the Working Group's experience, ICE Trade Vault already has such a process in place that is quite effective, especially when eConfirm is used. Even in the absence of eConfirm, a reporting counterparty should be permitted to confirm the accuracy of reported swap data upon submission as long as it has a confirmation in place with the counterparty with respect to the swap at issue.

B. The Proposed Rule Should Not Create an Obligation to Review Data Reported on "Dead" Transactions.

The Proposed Rule states that its "error and omission correction requirements would apply regardless of the state of the swap, and include the correction of swaps that are no

⁴ The Working Group understands that these issues might be addressed in one of the two forthcoming additional reporting related proposed rules. If that is the case, then the Commission should not move forward with the Proposed Rule until the other proposed rules are finalized and implemented.

longer open or `alive.'"⁵ The Working Group would like to confirm that this would require the correction of data submitted with respect to so-called "dead" swaps if such error is discovered, but would not obligate a reporting counterparty to actively review for errors in data reported with respect to "dead" swaps. If the Proposed Rule would create such an obligation, that would impose a material burden on reporting counterparties with little to no corresponding benefit.

C. The CFTC Should Clarify the Obligation of Non-Reporting Counterparties to Agree That Errors Exist.

The Proposed Rule appears to require that a reporting counterparty and a non-reporting counterparty must agree that a reporting error exists in order to trigger a reporting counterparty's obligation to correct erroneous swap data. Specifically, Proposed CFTC Regulation 45.14(b)(2) states that "[i]f...the reporting counterparty...and non-reporting counterparty...agree that the swap data for a swap is incorrect or incomplete, the reporting counterparty...must correct the swap data...."⁶

The Working Group reads this language as requiring both the reporting counterparty and non-reporting counterparty to agree that an error exists before the reporting counterparty has an obligation to correct that error and the Working Group would like the CFTC to confirm that understanding. If non-reporting counterparty confirmation is required, the Working Group asks that the Commission make clear that a reporting counterparty need only make reasonable efforts to seek a response from the non-reporting counterparty as to the existence of an error and may correct the error if the non-reporting counterparty does not respond.

D. The CFTC Should Allow for a Materiality Threshold for the Obligation to Report Reporting Errors to the Commission.

Under the Proposed Rule, a reporting counterparty would have three business days to correct a discovered error.⁷ If the error is not corrected within that period of time, the reporting counterparty must inform the CFTC of the error.⁸ The Working Group appreciates the Proposed Rule's inclusion of a period of time to correct errors. However, having to report an error to a regulator such as the CFTC is a serious matter, especially for a non-registrant. As such, the Working Group requests that the Commission (i) include a materiality threshold for the obligation to report out to the CFTC, and (ii) extend the period of time within which a report must be made to the Commission to ten business days for non-registrant reporting counterparties.

With respect to the materiality threshold, if a reporting error is limited in scope and severity, the reporting counterparty should remain responsible for correcting the error, but should not be required to inform the CFTC if they are unable to do so within the required time period.

With respect to the required reporting time period, three business days is far too short. Any report made to a government agency, especially one that relates to a potential regulatory shortcoming, is something that will be undertaken with caution and rigor. Such a report will require not only the input of the reporting counterparty personnel with technical knowledge

⁵ Proposed Rule at 21,069.

⁶ Proposed Rule at 21,099; *see also* Proposed Rule at 21,069.

⁷ Proposed Rule at 21,069.

⁸ Proposed Rule at 21,069.

of the reporting technology, but also compliance and legal personnel, and will typically need approval of senior management before its submission. For a non-registrant reporting counterparty, it would be difficult if not impossible to complete such a report in three business days. Further, if a reporting counterparty must simultaneously commit resources to addressing a reporting error and drafting the report to the Commission within a three day time period, resources that should be focused on curing the immediate problem—the reporting error—will be pulled away to work on reporting to the Commission. Therefore, the Working Group requests that the Commission extend the time period within which a report must be made to the CFTC from three business days to ten business days.

III. CONCLUSION

The Working Group appreciates this opportunity to provide input on the Proposed Rule and respectfully requests that the comments set forth herein are considered.

If you have any questions, please contact the undersigned.

Respectfully submitted,
/s/Alexander S. Holtan
Alexander S. Holtan

Counsel to The Commercial Energy Working Group