

21 September 2012

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Re: **Derivatives: OTC Central Counterparty Clearing**

Dear Sir/Madam:

Markit is pleased to submit the following comments to the Canadian Securities Administrators (the “**CSAs**”) in response to their Consultation Paper *Derivatives: OTC Central Counterparty Clearing* (the “**Consultation Paper**” or the “**CP**”).<sup>1</sup>

## Introduction

Markit is a provider of financial information services to the global financial markets, offering independent data, valuations, risk analytics, and related 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. In Canada, the major banks and an increasing number of hedge funds, asset managers, pension funds, fund administrators and other market participants use Markit’s products and services. We have a local office based in Toronto to better support our clients and we have dedicated substantial resources to establishing data and valuations services that will help Canada-based market participants comply with upcoming regulatory requirements.

Markit has been actively and constructively engaged in the debate about regulatory reform of the global OTC derivatives markets and the implementation of the Pittsburgh G20 commitments.<sup>2</sup> Over the last 18 months we have submitted close to 30 comment letters to regulatory authorities around the world, we have participated in numerous roundtables and we regularly provide the relevant authorities with our insights on current market practice, for example in relation to valuation methodologies, the provision of scenario analysis, or the use of reliable and secure means to provide daily marks. We have also advised regulatory authorities on appropriate approaches to enabling a timely and cost-effective implementation of newly established requirements, for

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<sup>1</sup> Canadian Securities Administrators, “CSA Consultation Paper 91-406 – Derivatives: OTC Central Counterparty Clearing” (June 20, 2012).

<sup>2</sup> “Leaders’ Statement: The Pittsburgh Summit” (Sept. 24-25, 2009), available at [http://www.g20.org/pub\\_communiques.aspx](http://www.g20.org/pub_communiques.aspx).

example through the use of multi-layered phase-in or by providing participants with a choice of means for satisfying regulatory requirements.

We welcome the publication of the Consultation Paper *Derivatives: OTC Central Counterparty Clearing* and we appreciate the opportunity to provide the CSAs with our comments. Specifically, we believe that (a) the determination which derivatives should be subject to a mandatory clearing requirement should be performed at a sufficiently granular level to reflect differences in liquidity; and (b) that any requirement for CCPs to publish clearing-related pricing data should be carefully calibrated.

## 1. The Mandatory Clearing Determination Should be Sufficiently Granular and Dynamic

We believe that the mandatory clearing determinations should be performed at a sufficiently granular level in order to reflect differences in liquidity between given derivatives transactions.<sup>3</sup> In order to reduce the time and effort that will be required to submit and approve the clearing determinations, however, they should be applied to “buckets” of tenors (*i.e.* groups of maturities and tenors for a given swap that have similar liquidity measures).

In this context, we believe that it will be important that (a) the liquidity of the derivative product or relevant category is measured with sufficient accuracy, and (b) such determinations are dynamic and are reviewed on a regular basis, but also ad hoc where necessary, over time. More specifically:

- We agree with other commenters<sup>4</sup> that the sufficient liquidity criterion should be applied conservatively and that further study will be necessary to determine if there is sufficient liquidity with respect to each derivative asset class. Establishing objective liquidity measurements that will be required as one of the inputs into the clearing determination can be a challenging task. Our experience as a provider of Liquidity Scores for a variety of financial products<sup>5</sup> has shown that they can be derived from a combination of observable factors including, but not limited to, trade frequency, average transaction size, bid/offer spread and the number of market makers. We would be happy to discuss these matters further with the CSA if it was helpful as part of its clearing-related determinations.
- Experience has shown that the liquidity of a given derivative product or even the entire market in certain circumstances can vary widely over time. As a result a certain type of derivative that trades actively today might quickly become illiquid in the future, and vice versa.<sup>6</sup> As the mandatory clearing determination should be reserved for the most liquid products, we agree with the CSAs’ proposal to potentially remove a derivative from mandatory clearing obligations if it is no longer suitable for central clearing, for example, when its liquidity dropped.<sup>7</sup> The CSAs’ clearing determination regime should include regular and frequent reviews of the mandatory clearing determinations to ensure equal regulatory treatment of similar products

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<sup>3</sup> We agree with the Committee that “whether there is sufficient liquidity in the contract” is key element for market regulators to consider when assessing whether an OTC derivatives contract should be subject to a mandatory clearing obligation. Section 3 Derivatives subject to a Mandatory Clearing Requirement. CSA Consultation Paper 91-406.

<sup>4</sup> ISDA Comment Letter in response to Consultation Paper 91-401 on Over-the-Counter Derivatives regulation in Canada (January 14, 2011)

<sup>5</sup> Markit provides liquidity measures, based on a number of relevant inputs, for a variety of OTC derivatives, bonds, loans, and structured finance instruments.

<sup>6</sup> Examples include a benchmark 10 year interest rate transaction after it turned into a 9 year and 11 month transaction in a month from now, or an on-the-run CDX credit index that will become an off-the-run credit index in 2 months from today.

<sup>7</sup> This is in concurrence with the CSAs’ statements that “If the result of the analysis shows significant deterioration to the [liquidity] factors, rendering a derivative no longer suitable for CCP clearing, market regulators will publish the findings and request public comment before making a decision on whether to remove the mandatory clearing obligation for such a derivative.” Section 3.2 Top-Down Approach. CSA Consultation Paper 91-406. Also See 3.2 Committee Recommendations. CSA Consultation Paper 91-406.

per the CSAs' clearing requirement and avoid situations where its determinations might trigger anti-competitive effects.

## **2. Requirements in Relation to the Transparency of Clearing-related Information Should be Carefully Calibrated**

The CP states that CCPs should divulge detailed information for market participants to evaluate the risks, costs and benefits associated with their participation in CCPs. This would include the disclosure of complete information on margin-setting methodologies, risk management arrangements and fee structure to actual and prospective users of CCPs.<sup>8</sup>

Markit has spent significant time and resources helping various CCPs around the world to establish procedures that assist in the determination of reliable daily clearing prices for transactions in OTC derivatives.<sup>9</sup> On the basis of our experience, we strongly believe that the CSAs should be careful to not require CCPs to publish certain pricing and valuations data. This is because such data will often only be provided to CCPs or to their participants on confidential terms and its publication would risk derailing the robust and tested process of determining the daily clearing prices that has been established over time for these products.

We therefore urge the CSAs to limit any requirement for CCPs to publish pricing data to the daily settlement prices for the most liquid contracts.<sup>10</sup> However, such requirement should not extend, for example, to price information or quotes that were provided to the CCP as inputs for their consideration. Further, consistent with the requirements that were proposed by the SEC, CCPs should provide access to their daily settlement prices on commercial terms that are fair, reasonable, and not unreasonably discriminatory.<sup>11</sup>

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Markit appreciates the opportunity to comment on the CSAs' Consultation Paper *Derivatives: OTC Central Counterparty Clearing*. We would be happy to elaborate or further discuss any of the points addressed above. In the event you may have any questions, please do not hesitate to contact the undersigned or Marcus Schüeler at [marcus.schueler@markit.com](mailto:marcus.schueler@markit.com).

Yours sincerely,



Kevin Gould  
President  
Markit North America, Inc.

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<sup>8</sup> Section 12 Reporting, CSA Consultation Paper 91-406.

<sup>9</sup> Markit Clearing provides official daily CDS settlement prices for multiple clearing houses around the world via Markit's website on a non-discriminatory basis. These settlement prices are used by the various clearinghouses and their members in their risk management processes. The settlements include both CDS single names across maturities and Markit CDS indices for the US, European and Japanese markets.

<sup>10</sup> In response to Question 9, "The Committee asks for comment on the type of information that a CCP should provide and that should be made publicly available."

<sup>11</sup> See Clearing Agency Standards for Operation and Governance, 76 Fed. Reg. at 14539 (to be codified at 17 C.F.R. § 240.17Aj-1) (published March 16, 2011).