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Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: Proposed rule: Trade Acknowledgment and Verification of Security-Based Swap Transactions (File Number S7–03–11)

Dear Ms. Murphy:

The International Swaps and Derivatives Association, Inc.[1] ("**ISDA**") is writing in response to proposed rule 15Fi–1 (the "**Proposed Rule**"), promulgated by the Securities and Exchange Commission ("**Commission**") in accordance with Section 764 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "**Dodd-Frank Act**"), which amended the Securities Exchange Act of 1934 (the "**Exchange Act**") by adding Section 15F, which among other things, requires security-based swap ("**SBS**") dealers ("**SBSDs**") and major SBS participants ("**MSBSPs**") to register with the Commission and directs the Commission to set forth rules applicable to them. The Proposed Rule would prescribe standards for the timely and accurate confirmation and documentation of SBS by SBSDs, MSBSPs and others (collectively, "**SBS Entities**").

ISDA respectfully submits the following comments in response to the Proposed Rule.

A. Trade Acknowledgment Requirement

The Proposed Rule places a heavy documentation burden upon the inception of transactions. This burden is far heavier than the burden on ordinary securities under the

[1] ISDA, which represents participants in the privately negotiated derivatives industry, is among the world's largest global financial trade associations as measured by number of member firms. ISDA was chartered in 1985 and today has over 800 member institutions from 54 countries on six continents. Our members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities. For more information, please visit: www.isda.org.

Commission's Rule 10b-10. The Proposed Rule also requires substantially more than is necessary to create an initial record of a legally binding agreement. We urge the Commission to consider that requiring more formality than necessary may lead to needless disputes and operational lapses. Requiring delivery of more information than is necessary similarly challenges operational processes and delivers to the Commission more information than it can possibly assimilate.

We think the proper role of the confirmation is that established decades ago in the SBS markets. The confirmation is a record of a trade: the confirmation may evidence a prior binding agreement or be a binding restatement of a prior agreement or be the instrument that effects binding agreement. Whether or not each and every transaction needs an "executed" confirmation containing certain information is initially a question of contract law. If the answer to the question of contract law is "no," then there is still room for prudential regulatory requirements, but only those that successfully balance costs and benefits. With this in mind, we suggest that the Commission reconsider its proposal as against the way the SBS markets now work. Is there actually a reason for 24 hour or less confirmation procedures? Should the "negative affirmation" procedure institutionalized in certain sectors of the SBS market be discarded? Does market nomenclature relating to the confirmation process need to change, to the certain confusion of market participants of every stripe? How are SBS Entities that are not registrants to be compelled to cooperate with the proposed process? We think these are fair questions that must be asked (and answered) if the Dodd-Frank regulatory process is to enhance the market and the economy.

We also note the lack of any history of abiding problems that require the "solutions" proposed by the Commission, or even any substantive study positing real associated risks to mitigate. We recognize that there may be a prophylactic aspect to regulation, but that aspect must be limited by a genuine cost-benefit analysis. We are not aware of any such analysis that would support much of what is contained in the Proposed Rule. The industry has moved, at great expense and in a targeted manner, to vastly improve the speed and efficiency of the post-trade documentation process *without loss of accuracy*. The process can be, and is being, continued in an equally targeted manner and with equal regard for the integrity of the post-trade process, but the process requires both time and meaningful goals. Please see footnotes 1-3 below (and accompanying text) for a discussion of some of the enormous improvements that the industry has produced in recent years in cooperation with regulators.

ISDA is also concerned about the generic "one size fits all" nature of the Proposed Rule. We note that the work done by the industry with the ODSG led to customization of documentation to account for the differences between asset classes, and even products within asset classes. In contrast, the Proposed Rule does not allow for this same flexibility. ISDA urges the Commission to take advantage of lessons learned by the industry. Rules for bespoke TRS, for example, may have good reason to be different from rules for garden-variety equity SBS.

B. Time to Provide a Trade Acknowledgment

The Proposed Rule sets forth the general principle that every trade must be followed by a "trade acknowledgment." A trade acknowledgment must be provided within 15 minutes of execution (for any transaction that has been executed and processed electronically) and within 30 minutes of execution (for any transaction that is not executed electronically, but that will be processed electronically). For any transaction that the SBS Entity cannot process electronically, the Proposed Rule requires that a trade acknowledgment must be provided no later than 24 hours following execution.

ISDA supports the Commission's objective of promoting the efficient operation of the SBS market and facilitating market participants' overall risk management. Indeed, ISDA has been at the forefront of industry efforts to prescribe standards for the timely and accurate confirmation of OTC derivatives for many years.[2] It is undisputable that documentation standards in the market have improved considerably[3] (including, but not limited to, the increased use of ISDA master confirmation agreements, standard terms and cross-asset matrices) to the point where it is now questionable as to whether the incremental benefits of the Commission's proposed standards for trade acknowledgments will outweigh the significant compliance costs that the Proposed Rule will entail.[4] Indeed, ISDA is concerned that the aggressive timeframes (24 hours or substantially less) embodied in the Proposed Rule may actually increase systemic risk by forcing market participants to focus on speed at the expense of accuracy. The Proposed Rule will also significantly alter the way end-users currently enter into SBS by potentially delaying their ability to execute SBS. This may hinder the timely execution of trades, an issue that is of paramount importance to market participants.

More fundamentally, certain terms required to be included in a trade acknowledgment simply may not be known to the transacting parties within 24 hours following execution. These may include counterparty name (if the trade is being allocated by an investment manager), initial rates and other important terms. Even if all information is known, the

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[2] Notably, pursuant to an effort led by the OTC Derivatives Supervisors' Group ("**ODSG**") of the Federal Reserve Bank of New York ("**FRBNY**"), market participants (including buy-side participants) regularly set goals and commitments to bring infrastructure, market design and risk management improvements to all OTC derivatives asset classes. ISDA is a participant in this project.

[3] The industry is meeting or exceeding ambitious agreed targets. In addition, by increasing automation and requiring end-users to obtain counterparty consent before assigning trades, the 14 largest credit derivatives dealers, pursuant to a joint regulatory initiative involving U.S. and foreign regulators after trading volumes in OTC credit derivatives grew exponentially between 2002 and 2005, reduced their total confirmations outstanding more than 30 days by 94 percent to 5,500 trades by October 2006. *See* U.S. Government Accountability Office, "Credit Derivatives: Confirmation Backlogs Increased Dealers' Operational Risks, But Were Successfully Addressed After Joint Regulatory Action," GAO–07– 716 (2007) at pages 3–4.

[4] Confirmation processing practices have been significantly enhanced by industry efforts in recent years and are continuing to be improved (*e.g.*, existing risk mitigants, such as the Economic Affirmation Process ("**EAP**"), a cross-asset, industry-agreed method of agreeing between parties of all key economics, and portfolio reconciliation, should already help to allay concerns of mismatched trade terms in the time period between execution and final documentation).

proposed timing standards are impractical for products where no "master confirmation agreement" or other similar template exists. It is also necessary to consider the Proposed Rule in light of requirements such as the need to include all "data elements necessary to determine the market value." Valuation procedures themselves will differ from party to party. To the extent they must be agreed, they will be heavily negotiated and are likely to be variable in response to specific transaction characteristics. Requiring the results of such negotiations to be reflected in data to be contained in trade acknowledgments will inevitably slow down the confirmation process (as well as the overall documentation process, to the extent that parties may be required to agree valuation procedures within their basic agreements).[5] In such circumstances, the preference of market participants would be to execute the trade in a timely manner instead of waiting for the conclusion of any negotiations related to non-economic terms.

Similarly, as mentioned above, ISDA is concerned that the 15- and 30-minute trade acknowledgment requirements may hinder the way that investment managers presently conduct their business. Investment managers commonly execute a single trade and then allocate positions across their clients. Frequently this process can take more than 15 or 30 minutes, or more than 24 hours, and frequently, the ultimate duration of this process hinges on receipt by investment managers of instructions from their clients, who would not be subject to the timing constraints set forth in the Proposed Rule. Without an appropriate exception that allows investment managers the time to allocate positions to their clients, those investment managers may be forced to execute individual trades for individual clients, thereby reducing economies of scale and increasing transaction costs for their clients. In addition, final terms (such as the "initial rate" in some circumstances) are unavailable for certain SBS until after execution. We urge the Commission to reconsider its proposed deadlines against these circumstances.

We also note that systems and practices for monitoring and recording of voice trade execution time do not exist, while cross-border transactions frequently necessitate more than 24 hours to deliver a trade acknowledgment due to business day and time zone differences. Based on these market realties, we encourage the Commission to adopt a flexible approach where the trade acknowledgment timing standard may differ based on asset type, trade type, counterparty type, event type and surrounding circumstances. ISDA suggests that the Proposed Rule should be delineated as follows:

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[5] We believe that the Commission's emphasis on valuation content in documentation between parties is misplaced. We believe that valuation data may be made available by other means. Please see our recommendation regarding valuation data set forth in the joint comment letter from ISDA and SIFMA to the Commodity Futures Trading Commission ("**CFTC**"), dated February 7, 2011, regarding the CFTC's notices of proposed rulemaking with respect to Real-Time Reporting, Swap Reporting and Recordkeeping by Swap Dealers and Major Swap Participants (*see* excerpt in Annex A hereto). A focus on valuation data at point of trade is misplaced.

(a) *Trades executed electronically and processed electronically*

As a preliminary matter, ISDA would request that the Commission clarify the meaning of a transaction that is "executed electronically" or "processed electronically." The bounds of these terms must be refined because there is a variety of systems and communication devices that may be used and that may have different assortments of features. It would be inappropriate to include within these terms all transactions for which some element of the transaction is captured or processed through electronic means.

Although the timeline set forth in the Proposed Rule may become workable in years to come, appropriate platforms and processes will need to be developed by the industry before that is the case. We also note that the term "processed electronically" is currently defined in the Proposed Rule by reference to the SBS Entity's computerized systems. Instead, we urge the Commission to define this term with reference to a trading facility's electronic processing system (or "middleware") which will actually drive the process. Electronic systems and platforms now available are not uniform and cannot uniformly comply with the Proposed Rule. Indeed, those systems may presently have difficulty communicating with each other. In this context, ISDA recommends that any externally imposed trade acknowledgment standards be both phased and aspirational.

ISDA would also encourage the Commission to provide that an SBS Entity could satisfy the Proposed Rule by executing an SBS on a swap execution facility or on a designated contract market, or by clearing the swap through a derivatives clearing organization. Such treatment would be consistent with the CFTC Proposal.[6]

(b) *Trades not executed electronically but processed electronically*

ISDA believes that it would be prudent to conduct a study in order to better understand the potential barriers to complying with any specific timeline in each asset class. For example, the equity derivatives market would have particular trouble abiding by the Proposed Rule as presently proposed to the extent part of the market relies on "negative affirmation," a contractual methodology relying on one-way confirmations that require no reply, unless terms are being disputed.

(c) *Trades not executed electronically and not processed electronically*

ISDA is concerned that the timeframes laid out in the Proposed Rule are not achievable based on current market practice. Transactions in this category are heavily negotiated, bespoke in nature and the post-trade detail work, often negotiated by lawyers, may be protracted. As applied to such transactions, the Proposed Rule set forth by the Commission would impose significant challenges and costs, particularly on end-users. Specifically:

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[6] *See* the principles discussed in "Regulatory Harmonization" below.

- Flexibility and "bespokeness" of contracts is key to enabling clients to execute the transaction types they require. Complete pre-agreement of terms would require end-users to engage significant legal resources for *all* proposed transactions, as compared to existing practice, which focuses on transactions that have actually been executed. It would also increase costs and so discourage end-users from hedging, all without any perceived benefit.

ISDA is generally concerned that the timeframes laid out in the Proposed Rule will impact the accuracy of trade acknowledgements sent. That accuracy is dependent on an investment of time in the internal controls that are part of the post-trade, pre-acknowledgment workflow.

Instead of rule implementation at this point, ISDA proposes a constructive approach similar to that utilized by the ODSG. This approach would involve an ongoing dialogue between the Commission and leaders in the SBS industry, with the goal of obtaining a commitment from the industry to tighten the trade acknowledgment timeframe over an extended period. As noted above, we believe that existing risk mitigants (*e.g.*, the EAP) may assuage the Commission's concerns in the interim.

C. Form and Content of Trade Acknowledgments

ISDA is strongly of the view that trade acknowledgement terms should be only the minimum required to evidence agreement to a trade and its material economic terms. Any extension of such requirements will lead to higher costs and an enhanced risk of administrative error. The Proposed Rule sets forth 22 specific items that SBS Entities would be required to provide in a satisfactory trade acknowledgment. ISDA is concerned that many items go substantially beyond the minimum requirement. These items for the most part will be present in the swap data repository ("**SDR**") so they should not be required on the trade acknowledgment. We also have other concerns about the following items:

(1) *Asset class*: standard taxonomy must be devised before this item can be effective.

(3) *Notional amount*: for equity derivatives, typical market practice is to confirm a quantity of assets (e.g., shares), rather than a notional amount expressed in monetary terms. ISDA believes that the Proposed Rule should account for this fact and thereby permit this practice to be maintained.

(4) *Date and time*: in the case of voice trades, trade execution times are typically not recorded. Fundamental workflow modifications and changes to market standards would be required to capture this information. We believe that regular securities transaction confirmations under Rule 10b-10 are not required to contain this information. On this basis, ISDA would ask the Commission to exclude this

information from the content required to be set forth in a trade acknowledgment under the Proposed Rule.

(10), (13), (14) *Identification of counterparty and counterparty status*: as we have commented elsewhere,[7] unless the Commission publishes counterparty status information, a dealer may not know its counterparty's regulatory status. We are also unsure why it is necessary or useful to note this information in the acknowledgment. As for particular "broker," trading" and "desk" identification information, we do not believe there is any analog under Rule 10b-10. In any case, as a point of practical implementation, we would expect this information to be maintained as central reference data that could be retrieved through the unique counterparty identifier held against the trade. Moreover, as noted above, the specific case where trades are subsequently allocated would have to be considered.

(11) *Existing SBS*: the type of "existing" transaction that is supposed to be the subject of this item is unclear to us.

(12) *Customization*: the trade identification aspect of a confirmation is usually fulfilled by inclusion of identification numbers provided by the parties, or by reference to a few salient characteristics (including date, notional amount and underlying) that are always in the confirmation. In other words, the identification purpose is easily satisfied. The proposed inclusion of elements necessary to calculate price may go substantially beyond the scope of what can or *should* be in a confirmation. Different entities may price in different ways, considering different factors. Elements affecting pricing may also be contained in other documentation between the parties. ISDA recommends that this standard be removed from the Proposed Rule given the breadth of information it potentially requires.

(15) *Payments*: contingencies of payment streams may be quite elaborate, and may be found in other documents, market usage and the like. Attempting to capture all such contingencies in trade acknowledgments will not be efficient or fruitful.

(17) *Market value*: please see our comment (on price) with respect to (12) above.

(21) *Venue*: we assume that the reference to "venue" is a reference to trading facility, if any.

(22) *Clearing-required information*: A counterparty will not need to see clearing agency instructions in an acknowledgment in order to feel comfortable verifying a transaction.

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[7] *See for example,* "Legal Entity Identifiers" in ISDA comment letter to the Commission and the CFTC, dated February 22, 2011, with respect to joint proposed rule regarding the definitions of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant".

D. Trade Verification

The Proposed Rule requires SBS Entities to promptly verify the accuracy of, or dispute with its counterparty, the terms of a trade acknowledgment that it receives. ISDA encourages the Commission to enter into a constructive dialogue with market participants to establish best practices for trade verification. Current market practices do not universally follow an acknowledgement/verification model. For example, for some products an acknowledgement or notice is sent for certain "mid-life" trade events without the expectation or need for a verification. In other cases (*e.g.*, for written confirmation of some new trades between major dealers), the convention is that both parties issue acknowledgements, only responding if there are discrepancies.

E. Regulatory Harmonization

ISDA supports the Commission's objective of promoting the efficient operation of the SBS market and facilitating market participants' management of their SBS-related risk. ISDA is concerned, however, that aspects of the rules proposed by the CFTC with respect to the confirmation of swap transactions and the reconciliation and compression of swap portfolios (the "**CFTC Proposal**") are inconsistent with the Proposed Rule in ways not related to the differences in the types of swaps under the jurisdiction of the respective commissions. This may lead to confusion in, and disruption of, the swap and SBS markets. ISDA urges the Commission and the CFTC to ensure that their respective regulations are harmonized as far as possible.

F. Cost-Benefit Analysis

In support of the Proposed Rule, the Commission states that an SBS Entity's development of an internal order and trade management system that ensures compliance with the Proposed Rule will cost approximately $66,650 per SBS Entity. Members of ISDA believe that this estimate very seriously underestimates the cost of implementing the Proposed Rule.

G. Extraterritorial Application

In the interests of maintaining the competitiveness of U.S. markets and U.S. SBS Entities, we believe that to the extent practices imposed on U.S. SBS Entities are different from and more burdensome than those imposed on equivalent entities in other jurisdictions, those practices should apply to U.S. customer business only. As we have stated previously, it is essential that U.S. regulations not hamper the overseas activities of U.S. SBS Entities. Nor should non-U.S. entities find access to the U.S. markets impaired.

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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 me or my staff at your convenience with any questions.

Sincerely,

Robert C. Pickel

Robert Pickel
Executive Vice Chairman

Annex A:

Excerpt from comment letter, dated February 7, 2011, submitted jointly by ISDA and SIFMA to the CFTC in response to the CFTC's notices of proposed rulemaking with respect to Real-Time Reporting, Swap Reporting and Recordkeeping by Swap Dealers and Major Swap Participants

". . . Longer term, the Associations recommend the creation of a "Counterparty Exposure Repository" as described below. We propose that this requirement would be in place of requiring valuation data on a transaction or swap level, which as discussed earlier is not possible due to the portfolio nature of collateral. Additionally, the computation of the mark-to-market value for a derivative position is quite complex for all derivatives. To perform this calculation one must be in possession of all the economic terms of a transaction (which may be over 100 data fields per trade) and all of the lifecycle structure parameters of a transaction, to permit the cashflow structure of the transaction to be constructed and the appropriate discounting and estimation of future value to take place. To perform these latter calculations, it is necessary to maintain a full set of current market data parameters, forward rates and the history of such market data. It is a computationally intensive and technically difficult task for each firm to compute the valuation each day for each transaction - all firms have invested significantly in the technology and staff to undertake this daily valuation, and even so it is not straightforward. Rather than the Commission duplicating these measures, we suggest that a data feed of general transaction data, plus the submitting firm's computed valuation, should be sufficient for market surveillance use, and will avoid the Commission incurring large expense in replicating existing computations. We note also that the prudential regulators of the SDs have the power (and frequently exercise the power) to review firms' internal valuation models, which would provide assurance that the valuation results being provided to the Commissions are sound, and would permit more in-depth analysis of valuation methods and parameters if necessary. . . ."