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Opening Remarks

A Buy-Side and End-User Perspective on the Safety and Liquidity of the Swaps Market  
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Good morning. I'm delighted to see such a large group of distinguished individuals come together today to continue a conversation that's been raging for the better part of two years – and doesn't appear to be slowing down at all. The reform of the U.S. financial system has been one of the most talked about, dissected and critiqued issues that I can remember in a long time.

And, of course, because we're in the financial services industry, Dodd-Frank has become something of an obsession for many of us. Every industry event I attend, every colleague I meet and every meeting I hold inevitably seems to veer into a discussion of Dodd-Frank.

This made me wonder how it compared to other news of late. So, I Googled "Dodd-Frank" recently and, sure enough, it turned up 6.28 million results. A similar search of the "Patient Protection and Affordable Care Act" – the President's healthcare bill -- generated only 653,000 results...and the Start II Treaty a mere 277,000 hits. Of course, I decided to take things one step further and Google...Charlie Sheen.

As you know, Charlie's been in the news quite a bit lately – and not surprisingly, it seems that he's of slightly more interest than Dodd-Frank. About 450 million more hits to be exact. I know, I know, it's hard to believe, but that tells me there's a lot more room for discussion of Dodd-Frank.

The goals of Dodd-Frank were to help the real economy and their participation in the over-the-counter (OTC) derivatives markets by better protecting them from loss and making their hedging markets more transparent and liquid....with aim of making hedging cheaper and more efficient. It is an untested assumption that the provisions of Dodd-Frank and the proposed rules there under will actually do this.

We have sponsored today's forum because we think these are important issues and ones where unintended consequences could be costly to the U.S. real economy. Therefore, we want to establish a dialogue on this subject. To that end, not only do we have speakers from both houses of Congress, including Chairman Debbie Stabenow of the Senate Agriculture Committee, but we have also brought together panelists from the regulatory community as well as the traditional and alternative investment management community.

We are happy that two buy-side industry associations, Institutional Investors and the Managed Funds Association, have agreed to cosponsor this event with us. We are particularly happy to have corporate end-users participating with us today, as well as money managers whose major accounts include real economy participants such as pension funds and corporates. The real question is how well a model based primarily on short-term instruments in a limited variety can be made to apply to markets roughly ten times the size, including a huge proportion of longer-term instruments with thousands of different underlying assets and securities. What features of this larger market implicate liquidity and in what ways?

## Thought Leadership

At DTCC, we've been hard at work building our own credentials with lawmakers and the regulatory community over the past two years as the balance of power in financial services has shifted from New York to Washington....and from London to Brussels. We've tried to stay one step ahead of this transformation because we recognize how important a role the infrastructure can play in a new regulatory environment. Over the past two years, many of our executives have logged countless miles on the Acela to meet with Members of Congress, the Administration, regulators, industry associations and others to educate them on DTCC....and to serve as a resource on the complex issues that have been under debate.

Today's conference is a reflection of DTCC's firm and solid commitment to its expanding role as a thought leader on these issues – and of its commitment to remaining a presence here in Washington. In fact, you may have already met our new head of government relations, Daniel Cohen, whose veteran status on the Hill makes him an important asset both for DTCC and also for policymakers. Dan just opened our new office here in Washington and he'll be available, as he likes to say, 24/7 to continue expanding on our role as a resource for Congress, regulators and interested third parties. Feel free to call at 3:00 a.m. on Saturday to make sure Dan lives up to his words!

## DTCC: Who We Are....What We Do

If we've done our jobs well these past two years, you should already know about DTCC and our nearly 40 years' experience as a market-neutral utility providing stability, certainty and reliability to global financial markets. I'll skip over our usual 30-second commercial on who we are to instead focus on the work we do in the OTC derivatives market, which will help frame part of today's forum. As you probably know, we don't clear OTC derivatives, but we do serve as the central swaps data repository – or SDR – and central life-cycle event processing facility for the global credit derivatives market. We call this repository the Trade Information Warehouse. Not only do we distill and publish a good deal of the data we collect in order to provide market transparency, we also give global regulators access to appropriate data to meet their own regulatory responsibilities.

The Warehouse's centralized repository and its users include all the major OTC derivatives dealers and more than 1,800 buy-side firms and other market participants in more than 50 countries. It holds virtually all CDS contracts globally, which amounts to approximately 2.3 million contracts with a gross notional value of \$29 trillion.

In addition to the Warehouse, which is based in this country, we operate a trade repository in the European Union. It's regulated by the Financial Services Authority (FSA) and was established, in part, to make certain that regulatory authorities in Europe also have assured access to key CDS market data. This subsidiary not only captures a mirror image of the CDS data that's held in the Warehouse, but it also serves as the global trade reporting repository for the OTC equity derivatives market.

In recent months, we've also introduced a new automated online tool. We call it a regulators' portal because it allows regulators and other authorities direct access to more tailored and detailed position reports from a global data set relating to their regulatory oversight requirements. To date, 20 different regulators worldwide have linked to this portal, which provides an unprecedented degree of market transparency by giving the authorities the type of granular data they need to protect against systemic risk, but also providing pre-determined filters to limit access to only that data in which they have an appropriate interest.

## Focus on Systemic Risk

The Warehouse is just one example of how DTCC has been tackling this issue for several years. In fact, it's just a small piece of the overall puzzle. We're working on multiple fronts to squeeze more risk out of the system to promote stability in global markets. Our recent initiatives include plans to accelerate the trade guarantee for

equities transactions, incorporating stress test results into clearing fund requirements, establishing a central counterparty for mortgage-backed securities trades, and launching a new clearinghouse with NYSE Euronext, known as New York Portfolio Clearing, to clear U.S. fixed income derivatives.

Here in Washington, the new Office of Financial Research is beginning to take shape with a broad mandate to monitor and mitigate systemic risk in the U.S. financial system. For example, DTCC and SWIFT have been working together to establish a global standard Legal Entity Identifier to support the OFR in its mission. This is a game-changer because the lack of a uniform LEI system across geographies and markets makes it difficult, if not virtually impossible, to determine the aggregate exposure of any single entity. A universal standardized LEI is the most effective way – and maybe the only practical way – to ensure data consistency across the industry. It will allow regulators to conduct analyses across markets, products, and regions to identify trends and emerging risks.

### Transparency Mitigates Systemic Risk

I offer this background because it relates directly to today's discussion. It also provides insight into the many different roles DTCC can play in ensuring a competitive, new market structure for OTC derivatives. We've been discussing this quite a bit recently. For instance, at the recent Congressional hearings on the implementation of Dodd-Frank, Don Donahue, our Chairman and CEO, and Larry Thompson, our General Counsel, testified on these matters.

I want to share with you the two main points they raised because, as the discussion of Dodd-Frank continues, they provide a roadmap for Congress and regulators to consult as they work their way through the bill.

First, the key to mitigating systemic risk in the swaps market lies in giving regulators transparent access to comprehensive market data. To underscore why this is so important, we need to rewind two-and-a-half years and look at how OTC derivatives contributed to the financial crisis. Broadly speaking, there was a general lack of understanding in the industry at that time regarding the extent of the exposures across all asset classes of the swap markets. This lack of understanding contributed to a lack of confidence in the creditworthiness of financial institutions at just the wrong time. The reality that the system to protect against such situations – and, by that, I mean the Trade Information Warehouse – was built prior to the crisis but did not contain the non-standardized mortgage-related swaps held by AIG for instance. It wasn't until after the crisis that the industry and regulators reached agreement to include these types of contracts in the Warehouse's data set. Because of this agreement, regulators today have sufficient early warning of the build-up of potentially risky positions – and they can take action to prevent a situation from spiraling out of control.

### Global Cooperation

The second point we stressed to Congress is that achieving transparency across the entire OTC derivatives market will require significant cooperation between market participants and regulators. Having spent countless hours working on this issue, I can tell you that our ability to create an integrated warehouse of CDS data would not have been possible without the substantial degree of global regulatory cooperation achieved through the OTC Derivatives Regulators Forum (ODRF) and the OTC Derivatives Regulators Supervisors Group.

Now, it seems to me that we're approaching a fork in the road, and the direction we take will have a profound impact on whether the goals of Dodd-Frank are fully achieved. If all sides continue down the path that produced the Trade Information Warehouse, we will ensure that regulators will have the tools they need to effectively mitigate risk in the OTC derivatives market.

However, if things veer off course and global cooperation can't be reached, we'll face a future in which data will be fragmented across numerous SDRs – and inaccurate reporting and double and triple counting of exposures will be commonplace. In this scenario, regulators and the public will be at a severe disadvantage when trying to get a timely, accurate and complete picture of the market. During a crisis, they will be even more

severely hampered. And the regulatory agencies will face the expensive and time-consuming task of having to build the complex data aggregation and reporting mechanisms that already exist – at a significant cost to taxpayers. Based on the industry’s experience, we believe that the SDR model used in the CDS market is the right model to be extended to the other asset classes of OTC derivatives. The infrastructure already exists and can be launched more quickly and cost-effectively than other potential solutions.

## A Delicate Balancing Act

The current reform environment is demanding that the infrastructure move closer to center stage because it holds the promise of helping the industry meet new mandates and reporting requirements in the most cost-effective manner. In playing this role, however, we are finding ourselves increasingly challenged to balance the competing demands of different stakeholders.

For example, how do we find the sweet spot of an issue when our owners may be pulling us in one direction, the regulators in another, and the buy-side in still another? It’s not easy, especially when we must balance these different interests with our overriding responsibility to remain vigilant to our mission of mitigating risk, reducing costs and enhancing efficiencies for the industry.

Interestingly, this same balancing act is being played out across the industry right now. Just look at the challenge facing the regulatory community in implementing Dodd-Frank. On the one hand, it needs to establish new rules and frameworks to address the vulnerabilities in the regulatory system that led to the financial crisis. On the other hand, it can’t create a new regulatory regime that is so burdensome that it encourages regulatory arbitrage across borders or weakens the competitiveness of the U.S. marketplace. I know the agencies fully understand the complexity of this challenge and are mindful of the potential for unintended consequences that could negatively impact our economy.

Forums like the one we’re holding today help identify issues of importance and outline potential elements of the solutions so that rule makers have the input and feedback they need to move forward. This collaborative search for answers reflects the somewhat symbiotic relationship between regulator and financial enterprise in the post-crisis world. After all, regulators want the financial services companies they supervise to be healthy and safe, and they know that firms cannot be safe and sound unless they earn strong returns.

As we’ve done for nearly 40 years, DTCC will play a critical role in this process by providing the stability and certainty that’s essential for robust markets. Whether you’re a regulator or an end-user, a buy-side firm or a policymaker, or any of the other countless participants in the financial markets, we all share a common goal for the future – that we have strong regulatory rules to protect the financial system and investors.....and that the U.S. markets remain the most liquid, efficient and competitive in the world.....that they nurture ingenuity, innovation and creativity.....facilitate capital formation.....and serve as the engine to long-term economic growth and prosperity. At DTCC, we believe we can help regulators and the industry achieve that delicate balance.

## Closing

I’m certain we’ll hear a lot more about all of this throughout the day. And I have no doubt that our first panel on liquidity will be informative and help establish the type of dialogue we can facilitate here in Washington.

But before I turn the podium, let me again thank everyone who is joining us today. And I want to give a special thanks to Danny Faryniarz, Gregg Rapaport and a team of dedicated people at DTCC, MFA and Institutional Investors for putting today’s forum together.

Let me now hand it off to John Gidman of Loomis and Sayles, who will introduce the Liquidity Panel. Thank you.