



January 23rd 2009

Via e-mail to secretariat@cesr-eu.org please respond to tony.freeman@omgeo.com

The Secretariat
Committee of European Securities Regulators
11-13 avenue de Friedland
75008
Paris
France

re: Consultation on CESR/ESCB draft recommendations for securities settlement systems, and
draft recommendations for central counterparties

Dear Sirs

Please find below our official response to the above consultation. Please do not hesitate to contact us if you require any clarification.

About Omgeo

Omgeo is one of the largest providers of trade confirmation systems globally. Our focus is on transactions executed by institutional investors both on-exchange and OTC in domestic and x-border markets. Our client community includes investment managers, broker/dealers and custodian banks. We have more than 1,000 clients in Europe and more than 6,000 globally. Omgeo systems process in excess of 1m transactions daily.

Omgeo is a global joint venture equally owned by The Depository Trust & Clearing Corporation (DTCC) and Thomson Reuters. Our principal products are: Omgeo CTM (Central Trade Manager), Omgeo Oasys Global and Omgeo Alert. For more information go to www.omgeo.com

Response to Recommendation 2 – Trade Confirmation & Settlement Matching and Recommendation 3 – Settlement Instructions

The strategic importance of the middle-office. Omgeo clients operate our systems principally in the middle-office. The middle-office is a strategically important function that has not historically

received sufficient attention in the policy debate on clearing and settlement issues. The increased volume and sophistication of trading in recent years has not been matched by similar improvements in the operational capacity in the middle-office. Huge increases in volume and increased ability to execute smaller trades have placed strains on many buy and sell-side firms. The principal objective of the middle-office is to capture and disseminate accurate trade details in a short timeframe. It is clear that the accuracy of this function drives downstream efficiency. It is not possible to maximise efficiency and minimise risk without having an accurate near real-time picture of what has been traded. The middle-office, and the trade-confirmation process, therefore deserves close attention in the policy debate in this area.

The mechanics of trade-confirmation. There are many different ways of achieving a confirmed-trade. The two basic mechanisms are:

- Confirm/Affirm: a process where broker/dealers sequentially enter date to a central system and investment managers agree or disagree the trade
- Central Matching: a process where both the broker/dealer and investment manager enter trade details which are then matched by an algorithm at a central system

Both methods are effective tools for agreeing a trade. Omgeo operates both confirm/affirm systems and central matching systems. Our data indicates that central matching produces more accurate confirmations in a shorter time-frame. (Data on this issue was supplied in our earlier letter to you of June 19th 2004.) Many other vendors operate similar systems.

Irrespective of the methodology used, all trade confirmations follow a similar workflow:

- internal booking of the block-trade (what was traded) and allocations (what will settle) from dealer/fund-manager
- receipt of the block-trade instruction from the broker/dealer counterparty
- transmission of the allocation instructions to the broker/dealer counterparty
- receipt of the trade confirms (the combined block and allocation details) from broker/dealer counterparty (the confirm will contain the final economic details and the settlement instructions of the trade)
- agreement by the investment manager that the final confirm is 100% accurate
- delivery of the allocated trade to the appropriate custodian bank responsible for settlement
 - o as stated above the agreement (or verification) of the trade can be achieved by a confirm/affirm process or a central matching process
 - o it is also normal for standard settlement instructions to be added to a trade as it flows through the confirmation process: a function generally referred to as “enrichment”
 - o this process is applicable to exchange-traded and OTC transactions and applies similarly to domestic and x-border transactions

The speed and accuracy of the process described above varies widely. We refer to SDA (Same Day Affirmation) as the operational standard that all market participants should aim for. SDA is the completion of the trade confirm process on T+0 (the execution date of the trade). We have presented our data on SDA on many occasions and it was the subject of the Oxera study, commissioned by Omgeo, in May 2008. Many Omgeo clients achieve SDA in less than 3 hours. For those clients using the central-matching workflow more than 90% of trades achieve SDA.

Conclusions

Omgeo believes that SDA is a catalyst for improving post-trade processing efficiency and is the cornerstone of operational accuracy, efficiency and risk reduction. This is a principle agreed by all parties, but is not universally achieved. Some market participants have not automated their trade confirmation processes and use a variety of ad-hoc communication mechanisms (such as fax, email, telephone) to liaise with their counterparty. Apocryphal data suggests this may be as much as 20% of the overall volume in the customer-dealer market. Broker/dealers have also been vocal about the cost differential between customer transactions and dealer-dealer transactions. It is widely accepted that approximately 75% of all on-exchange activity is dealer-dealer. The remaining 25% is dealer-customer. For most broker dealers, the costs are inverted: 75% of all operational cost is derived from customer transactions. This is primarily caused by manual clients. This represents a considerable unnecessary level of risk and cost to the overall market.

Recommendations

Below are our direct responses to recommendation 2.

- a) There should be no differentiation between direct and indirect market participants. This delineation is somewhat artificial and does not take into account the levels of risk in the market. An indirect market participant such as a leveraged Hedge Fund executing a very high volume of transactions represents a much greater risk than another dealer

There is also no evidence that indirect-market participants (buy-side firms) are structurally unable to achieve the highest standards of process accuracy and efficiency. As stated earlier, many Omgeo Investment Manager or Buy-side clients achieve SDA in less than 3 hours.

- b) Interoperability between providers of trade confirmation systems is complex and has largely been obviated by usage of middleware and message transformation technology. Most buy-side firms have the capability to manage data in different formats and innovation in this sector has not historically relied on usage of messaging standards or interoperability agreements between vendors. Industry experience also indicates that interoperability projects often have an unclear return on investment.
- c) Regulators should focus on the operational standard that is good for the market, and not mandate a single method or solution. There are many different ways of achieving SDA. The approach of setting operational targets has been very successfully employed by the Federal Reserve in its project to raise operational standards in the OTC derivatives market. In cooperation with the OMG (Operations Management Group) committee, representing buy and sell-side participants, operational targets have been defined, measured and consistently made more stringent. The improvement in operational efficiency and risk reduction has been facilitated by multiple vendors working in cooperation with OMG and ISDA (International Swaps & Derivatives Association) representing market participants. This project has been a significant success in a short timeframe and has been achieved without any formal regulation. It appears that the threat of regulation has been the primary driver. It is also very important to note that this process has been international – although the Federal Reserve is the leader of the project it has been encouraged by several European regulators where it has been equally successful.

Our principal recommendation is therefore to place as much emphasis on the middle-office as well as the downstream clearing and settlement area. Recommendation 2 addresses the key process of trade confirmation which we, and our clients, believe drives downstream efficiency. Significant improvements in overall market risk and efficiency can be generated by market-wide adoption of best-practice in this area.

Please do not hesitate to contact me for any clarification or further detail of the content of this letter. I am happy to meet with you at any time.

Yours faithfully

A handwritten signature in black ink, appearing to read 'A J Freeman', is positioned above a thin, light blue vertical line that extends downwards.

Tony Freeman
Executive Director – Industry Relations, Omgeo Ltd