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ISDA®
INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC.

Mr Toby Wallis
Primary Markets Policy
Financial Services Authority
25 The North Colonnade
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London E14 5HS

23 January 2009

Dear Toby

RE: FSA CP 08/17 Disclosure of Contracts for Difference

This is a response to the referenced CP being made on behalf of the London Investment Banking Association (LIBA) and the International Swap Derivatives Association (ISDA).

We appreciate the opportunity to respond to the CP on behalf of our Members. We note that this CP culminates a long period of consultation dating from 2007. During this period, we and our members have had the opportunity to meet with you and your team to discuss various salient issues which has been useful to both our members and your team.

Broadly speaking, our members believe that the proposed disclosure regime for CFDs will be more intrusive than in any other major financial centre. As proposed, it is aimed at certain parties who are said to have unfairly pressured the management and boards of publicly listed companies on the basis of alleged de facto control of shares through unreported long positions in CFDs or similar derivatives. The proposed regulations will require investors to disclose their aggregate holdings (long) in shares and derivatives once the trigger level of 3% is reached and, thereafter, at each 1% interval.

We strongly support the exemption from the disclosure regime which is proposed for market makers of shares and regulated dealers who trade in CFDs in a client serving capacity. A similar exemption is contained in the Transparency Directive and in the UK Takeover Code, and the proposed exemption recognises the fact that market makers and client serving dealers provide the essential liquidity to their respective markets. In doing so, they face substantial trading risk which would be increased if they were required to disclose their positions to competitors. Increasing the trading risk of market makers would lead less liquid markets.

We have written separately to you regarding the need to recognise that hedging is part of market making and part of client serving dealers and should be considered to be under the

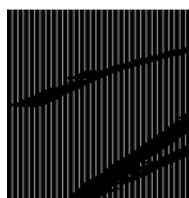
10% exemption for market makers. This is the current practice and understanding in the market, our members also hold that hedging activities undertaken against proprietary trading positions should be counted under the 5% exemption from the disclosure requirements for proprietary trading accounts.

We must note our strong preference for a September 2009 implementation date as was indicated in the CP. The consensus is that a significant shortening of the implementation period as has recently been indicated would severely impact our members' ability to meet important planned commitments. As a result of the current crisis, our members are struggling with numerous systems projects which are required to meet regulatory requirements and business exigencies. Thus, meaningful accommodation will be required to ensure that compliance with any new regulations will be a practical possibility. For this reason it is essential that required disclosures on a nominal basis be allowed. Also, convertible securities (which have not been reported as being used in a problematic way) should be excluded from the disclosure regime to make systems development more straightforward by eliminating the need to program conversion ratios and the resulting outstanding shares total. This would not increase the likelihood of avoidance because convertibles are a much more costly surrogate for shares than are CFDs or other derivatives. Lastly, the removal of any requirement to systematically separate hedging from market making accounts against which the hedge is being established would streamline the systems implementation process as well as maintain the current practice of market makers.

Attached are answers to the specific questions posed in the CP.

Thank you for your consideration of this response.

Very truly yours



William J Ferrari	Richard Metcalfe
Director	Head of Policy
London Investment Banking Assoc	International Swaps and Derivatives Association

About our associations:

LIBA is the principal trade association in the United Kingdom for firms which are active in the investment banking and securities industry. The Association represents its members on both domestic and international aspects of this business, and promotes their views to the authorities in the United Kingdom, the European Union, and elsewhere. More information LIBA is available at www.liba.org.uk

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 56 countries on six continents. These 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 financial market risks inherent in their core economic activities. Information about ISDA and its activities is available on the Association's web site: www.isda.org

RESPONSES TO CONSULTATION PAPER

Q.1 Do you agree that our approach to definition and scope will be a workable solution that will give the market sufficient certainty while restricting attempts to avoid disclosure?

A.1 In general, we do agree with the approach to definition and guidance which is indicated in the CP. In particular we consider that the treatment of any internal movement of a position between accounts for tax/accounting or other internal reasons is sound as is the principle that other financial instruments having similar economic effect to a qualifying financial instrument should be subject to disclosure according to the same terms. The treatment of derivatives referenced to a basket of shares seems a practical approach (1% of issue class and 20% the basket's value).

Q.2 Do you think that our rules and guidance requiring disclosure on a delta adjusted basis would meet our objective of countering possible anti-avoidance issues and preventing over-disclosure of national interests in cash settlement derivatives?

A.2 While we do understand the logic of a delta adjusted disclosure regime, our members have indicated that firms actually use a variety of delta calculations around different types of derivatives which could lead to confusion in the mind of the user. Also the systems work needed for the necessary calculations in the aggregation process will be quite complex and expensive. Our members have pointed out that the delta adjusted regime for short selling disclosure , which is now in place, is aimed at a very restricted number of issues and involves the intervention by staff who must meld the firm's disclosure and risk systems manually to create an accurate disclosure. To do this for all cash settled CFD/derivatives would be a much more onerous undertaking. Thus, it is not safe to rely on firms' compliance with the limited short sale regime as a basis for assuming that compliance with the much broader regime on a delta adjusted basis will not require systems development and additional resources.

We propose that disclosure be allowed on a nominal basis. This will allow a simpler/quicker systems development approach to implementation of the disclosure regime.

Q.3 Do you agree with our approach to having an exemption for client-serving transactions?

A.3 We strongly agree with the exemption for client-serving transactions which will allow market makers of securities and regulated derivatives dealers to provide liquidity to the market without the increased trading risk which disclosure to the market would create. This would approximate the exclusion which exists in the Transparency Directive and the UK Takeover Code. It should also be remembered that regulated market makers and CFD dealers have not been identified as parties seeking to acquire surreptitious stakes in companies or to pressure management or boards of relevant companies. We understand that the ABI, CBI and IMA share the view that regulated dealers have not been part of the perceived problem.

Q.4 Will that exemption be effective in reducing the number of unnecessary and misleading disclosures, without significantly increasing the risk of avoidance of disclosure?

A.4 As discussed in 3 above, we believe that the exemption for client-facing activities of regulated market makers and dealers will result in reducing unnecessary and misleading disclosures, and the exemption would not significantly increase the risk of avoidance of disclosure.

Q.5 Do you agree that our approach to group issues is a practical and workable solution?

A.5 We agree that non-EEA companies in the same group as a UK authorized market maker or derivatives dealer which have equivalent authorizations from their relevant regulator should be allowed in principle to be treated in the same way as their regulated UK affiliate under the proposed disclosure regime. However, we suggest a more efficient and flexible

approach to the certification of such non EEA companies. We propose that the FSA would accept the written representation of an officer of the UK regulated company that specified affiliates meet the necessary qualifications and undertaking on behalf of the UK regulated company to inform the FSA in the event of any relevant change in the status of any of its specified affiliates. This would obviate the need for arranging formal letters from each non EEA company which will be time-consuming and subject to formalities. However, the FSA would be in a position to request additional relevant information from the UK regulated company with respect to the status of a specified affiliated company if it is deemed necessary and to withdraw the accommodation of a non EEA affiliated company where it is deemed by the FSA to be necessary.

We would suggest removing the words "is not able to" from proposed R.5.3.1 (3)(c) (I), since owning shares confers the right to vote them , even where an investor has determined not to do so.

Q.6 Do you agree with our approach to applying the existing DTR exemption to CfDs?

A.6 We have written to you separately regarding market making and the hedging of positions taken as a market maker or client-facing dealer in derivatives (see our letters to Toby Wallis dated December 5th and 12TH 2008). In general out view is that a hedge position is part of the market making trading book when it is taken to offset a position taken as a market maker or as a client-facing dealer of derivatives. Likewise, positions taken as hedges of proprietary trading positions should be part of the proprietary trading book.

To explain: When a CFD dealer writes a CFD in executing an order for a client, it may hedge its resulting financial obligation to the client by buying the shares referenced in the CFD. If so, it is clear that the purpose of the hedge is to facilitate the client facing activity. Clearly, the purchase of shares is not for the firm's own investment purposes i.e. not for its proprietary trading purposes. But for the execution of a client's order, there would have been no purchase of the shares.

We note that under current and proposed regulations, a market maker may hedge a short position in a delivery option by purchasing the relevant shares without any disclosure being required unless the 10% trigger were breached after netting the share positions. Yet under the proposed regulations, a market maker would have to consider a hedge of a short share position using a CFD long position by reference to the 5% trigger for disclosure purposes without netting. This is an anomaly which would be avoided if hedging activities were treated as they currently are by market makers.

Note that considering hedging activity as part of the trading book being hedged would also avoid duplication of disclosures e.g. where the holder of a hedge CFD position discloses its long holding and the purchaser of the related short sale of securities reports his long position in shares (borrowed by the short seller who is holding the CFD).

For these reasons and those indicated in the referenced letters, we take issue with para 3.44 of the CP which characterizes all hedging activity as proprietary.