



13/04/2005

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Dear Andrew,

**Response to the SWIFT Consultation for "The Proposal For The Removal Of Barrier 1 Of The Giovannini Report"**

## 1. Preamble

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virt-x welcomes the publication of the consultation paper outlining the proposals to remove Barrier 1 of the Giovannini Report and for the opportunity to input into such an important element of the wider European harmonisation process.

We are pleased that SWIFT has accepted this challenge and is transparently interacting with the market to seek views and, ultimately, to agree a plan of action for the removal of this barrier.

This is a response on behalf of virt-x Exchange Limited, a UK Recognised Investment Exchange, supervised by the Financial Service Authority and an SWX Group Company. The views of SWX Swiss Exchange, the Swiss Stock Exchange supervised by the Swiss Federal Banking Commission and also an SWX Group Company are given within the response from the Swiss Commission for Financial Standardisation (SCFS).

## 2. Background

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Historically the utilisation of domestic proprietary links and messaging standards to (I)CSDs has prevented or restricted widespread access to these services for a number of market participants. The original Giovannini Barriers identified this as one of the key items preventing European harmonisation. However, since the Giovannini report was originally published there have been some developments to open these proprietary links to greater internationalisation. An example of this is that Crest now offers connectivity to its services by means of the ISO15022 SWIFT standards and messaging, whilst still supporting its proprietary links. Whilst these developments, throughout the European landscape, should be taken into consideration as part of the SWIFT consultation it must be remembered that one of the prime reasons that, following the earlier example, the proprietary link is retained is due to the current limitations on messages resulting in the inability to support the plethora of transaction types required to fully support a participant's business activities.

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### 3. General

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We support your assertions that any standards derived from this exercise should not be limited to Continental Europe or indeed to the EU itself. The standards must be capable of use within the global market to achieve a truly viable long term solution.

We do not believe that any new message standards should be limited to use within the SWIFT network. In the spirit of harmonisation and end user choice these messages could and should be available to other network providers and more generally to providers of messaging services as determined by users.

We would strongly urge you to conduct this consultation process in an open and transparent manner which would help to assuage the concerns of members and demonstrate that you are working to benefit the wider community without bias towards SWIFT itself. The creation of a consulting group drawn from the widest possible audience across Europe, including representative bodies from the different jurisdictions and, importantly, other network suppliers would also help along these lines and would give you valuable buy-in as you progress towards the ultimate solution. The initial delivery of your consultation paper to a wide audience has been a good start in this respect.

We suggest that domestically the users and regulators of the infrastructures could place pressure on these providers to upgrade their interfaces to adopt message standards especially when opportunities to enhance services arise and technological upgrades are required. In these instances the prolongation of proprietary links should be avoided or at least should not be maintained at the expense of common standards.

The review should help to identify which areas would deliver most benefit to the end users and therefore assist in prioritising future work. Naturally a 100% success ratio is the ultimate goal but if demonstrable benefit can be derived following an 80/20 rule this should be adopted and should also give additional impetus to the end goal.

As you are aware the Euroclear harmonisation process and development of Common Communication Interface (CCI) will have a significant impact on your deliberations and will most likely run in parallel to each other. It is imperative that these two initiatives do not deliver widely divergent solutions and that they are both implemented within a short timescale. If there were to be a significant difference in the implementation schedule it is possible that the "first past the post" solution could become the European solution by default.

Additionally to maximise success on this initiative you must ensure that there is close co-operation with CESAME and that you co-operate and leverage the vast amount of work already undertaken by ECSDA, specifically in relation to corporate actions harmonisation and the creation of a standardised "data dictionary" by which we mean a common understanding of data sets, their use and impact. (e.g. common understanding and use of items such as record date or ex-dividend date)

Finally the implementation of ISO15022 standards was a major transformation impacting both participants and infrastructure and we assume that not all participants are yet full compliant. Under these circumstances it is difficult to imagine that participants will now, within such a short timeframe, wish to move to an ISO20022 standard to fulfil this proposal and we suggest that ISO15022 should be the standard on which this project progresses. However, we accept that if there is no current standard for a particular message type then a new standard should be developed in ISO20022.

### 4. Specific Responses

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#### 4.1 Section 3

*1. Do you agree with the scope of the solution as defined? If not, please define your suggested amendment and explain why it is required.*

*2. Is there a more likely structural scenario that would make the implementation of a common protocol redundant? If yes, please define your scenario and explain why it is more likely and how it makes the protocol redundant.*

We agree in broad terms with the scope of the proposal and that it should be unambiguous to ensure there is a clear and common understanding of what is being addressed and importantly what is not addressed. Further definition on this aspect should be conducted during this consultation phase.

The key drivers of increased market safety, improved efficiency and reduced costs should be the criteria used at each stage of analysis and development to ensure these are being delivered throughout the process. Qualification of these drivers may well lead to an adjustment in scope, in either direction, throughout the process.

We support the assertion that the standard should be instrument neutral however, given the different nature of financial instruments this may result in potentially different standards required to support different instrument characteristics. For example not all traded instruments have ISIN codes. We also support the assertion that all participants, integral to the service, should be included within scope and not limited to infrastructure providers (i.e. (I)CSD).

## 4.2 Section 4

*1. Do you believe the nine protocol elements correctly frame a potential communication protocol? If “not”, please specify the elements you would include/delete and why.*

Section 4.1, diagram 2 would have greater impact and clarity if the picture showed the vertical pillars of Standards, Security and Service within the diagram and not just within the later explanation. Additionally it would also benefit if the network layer was shown as potentially independent of the data or messaging layers.

*2. Do you agree that the features of each protocol element are defined correctly? Are there additional features you believe should be part of the mandatory baseline, e.g. should message archival and retrieval be a mandatory feature of the messaging service element? If so, what are these features and why should they be included? Conversely, are there any features which are defined within the mandatory baseline that you believe should not be included? If so, what are they and why should they not form part of the baseline.*

We remain unconvinced that modelling is needed for all processes specifically commencing from pre-trade (Section 4.2.1.1, 1, paragraph 2) as this is an area which has seen some significant initiatives over the past few years, some of which failed to reach fruition. There could also be a misunderstanding that this initiative should drive the business process and this would be the wrong way around. We would urge SWIFT not to extend scope significantly and try to achieve too much which could be detrimental to ultimately achieving the main goal.

*3. Should a minimum set of performance standards be quantified for each Service element? If yes, what is the minimum acceptable content and how would you quantify it, e.g. Service should be open 24x7 with 99.999% availability.*

The performance standards for a service provider (SLA) should be set between the participant and supplier as in any normal set up of this type of commercial relationship. However, a recommendation of best practise could be a successful methodology to allow users to identify minimum service level requirements.

*4. Which of the mandatory features identified above have you already implemented?*

The quality of services offered and the levels of service support available by a supplier are standard items reviewed during an RFP.*5. What is your opinion of the need to implement a market wide Data Standards compliance commitment, i.e. when new data standards are published, all participants agree to implement within specific timeframes. If you agree, is a 6 month mandatory compliance window appropriate? i.e. compliance with the standard is mandatory within 6 months of publication.*

A common compliance window to adopt new standards should be developed and clarity should be given to all participants when expired messages will no longer be supported. However, it is clear that there will not always be a definitive cost benefit for all participants to adopt new standards simultaneously. This could be handled by timelines being set in line with “majority” adoption but as the messages would be used by multiple network providers it is unclear at this stage how compliance could be policed across the markets. However, it is clear that unless the standards are regularly maintained and updated this could create divergence and impose restrictions on interoperability which would be

counterproductive to the whole initiative albeit the rise of the internet and the freedoms it allows users could well negate some of these concerns in the longer term.

*6. What is your opinion on the mandatory outsourcing of dispute resolution and commodity services to the provider[s] of messaging and/or network facilities? If you agree that outsourcing of such services should be mandatory, what services should be considered:*

- appropriate to dispute resolution
- as commodities

We do not agree that this subject must be mandated to the providers of the services. Dispute resolution is conducted today between the customer and provider and is often addressed within an SLA. The implementation of new message standards should not necessarily alter this fundamental aspect of a relationship. As mentioned in question 3, best practise requirements would assist users in this regard.

*7. Do you agree that an independent accreditation of Messaging/Network suppliers is required to guarantee the conformance of suppliers to the stated baseline functionality? If no, should there be a single provider of Messaging and Network services for European Clearing & Settlement? If yes, who should provide this accreditation facility?*

As stated earlier we do not believe there should be a single network provider within this area and therefore if the network should be directly within the scope of this initiative. Accreditation could not then be supplied by a single source and could only be delivered by either the network or the infrastructure provider. However if accreditation is to become common it must not distort or hinder competition or freedom of access to any participant.

*8. If you do not agree with either accreditation or single service provision, how do you believe compliance with the baseline functionality should be monitored and maintained?*

*Not applicable*

*9. Should the providers of Messaging and Network functionality police the quality of traffic against the defined standards? (Note, this requires the service provider to 'read' content) If yes, should they be empowered to stop traffic that does not conform to agreed standards or merely report on non-conformance?*

We would not support the requirement for a network service provider to read message content. However, as a baseline it would be acceptable for providers to validate message formats rather than content. The policing of the message standard itself could be undertaken between the communicating parties to drive out inconsistencies and deliver improvements to the participant usage. This should be common practise between a participant, service provider and infrastructure. Compliance towards message standards should be maintained by pricing. e.g. if a participant supplied an incorrect message format to its custodian resulting in a manual correction on the part of the custodian then the custodian often charges an additional fee to cover this inefficiency. This in turn should drive compliance as it is cost effective to do so.

*10. Is the minimum security level defined at the messaging layer appropriate to all communication:*

- a. generic/non binding information exchange such as end of day price distribution.
- b. binding information exchange such as statements, status reports notifications etc.
- c. business critical information exchange such as instructions and confirmations.

*If not, what should the minimum level of security be for each type of information exchange?*

In line with earlier comments that network provision would be open to competition this aspect could equally be open customer need. Greater levels of security may be beneficial to different participants and could be a "value added" service by the provider.

## 4.3 Section 5

*1. What is the industry view on establishing two distinct goals, effectively phasing the implementation of the solution:*

- a. A short term system interoperability goal to be achieved within an agreed timeframe, e.g. two years?

*b. A long term business interoperability goal to be achieved within an agreed timeframe, e.g. five years?*

We accept that the timescales surrounding this initiative as defined by Giovannini are extremely optimistic. We would support a phased or modular approach which is capable of delivering demonstrable end user benefits within acceptable cost boundaries from the outset whilst a longer term goal was being further developed. One assumes that as the implementation of any agreed standards will no longer be the remit of SWIFT that this implementation phase would be a longer term goal.

*2. If such a phased strategy is appropriate, what would be considered to be acceptable time frames for achieving each goal?*

We suggest that further analysis is conducted to identify the eventual framework before timeframes are attached to the initiative.

*3. If such a strategy is inappropriate, what is the industry view on a more acceptable solution and why?*

Not Applicable

*4. What mechanisms should be used to encourage take up of the recommended protocol within agreed timeframes, e.g. mandatory migration, financial penalties etc.*

As stated in earlier responses a mixture of both mandatory migration and cost pressure could be applied to ensure adoption of the agreed solution.

*5. What is the industry view on the standards co-existence requirement outlined above? Does such a strategy adequately support the ongoing improvement of the Clearing & Settlement process? If not, what alternatives exist?*

A common compliance window to adopt new standards should be developed and clarity should be given to all participants when expired messages will no longer be supported. However, it is clear that there will not always be a definitive cost benefit for all participants to adopt new standards simultaneously. This could be handled by timelines being set in line with "majority" adoption but as the messages would be used by multiple network providers it is unclear at this stage how compliance could be policed across the markets. However, it is clear that unless the standards are regularly maintained and updated this could create divergence and impose restrictions on interoperability which would be counterproductive to the whole initiative albeit the rise of the internet and the freedoms it allows users could well negate some of these concerns in the longer term.

If you have any questions arising from our response or require further explanation on our comments please do not hesitate to contact either:

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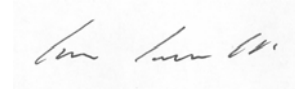
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We are convinced that this first piece of work is a solid base on which to move forward and we look forward to participating in the next stage of this important and exiting initiative and to the discussions and future consultations which will undoubtedly follow from this inaugural phase; to drive out more detailed descriptions, activities and plans.

Yours sincerely



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