Supporting Statement for
Semiannual Report of Derivatives Activity
(FR 2436; OMB No. 7100-0286)

Summary

The Board of Governors of the Federal Reserve System, under delegated authority from the Office of Management and Budget, proposes to extend for three years, without revision, the Semiannual Report of Derivatives Activity (FR 2436; OMB No. 7100-0286). This voluntary report collects derivatives market statistics from seven large U.S. dealers of over-the-counter (OTC) derivatives. Data are collected on notional amounts and gross market values of outstanding OTC derivatives contracts for broad categories of market risk: foreign exchange, interest rate, equities, commodities, and credit. For the different types of market risk except commodities, further detail is collected on the underlying market risk of each contract-- the underlying currency, equity market, or reference entity (borrower).

This collection of information complements the triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity (FR 3036; OMB No. 7100-0285). The FR 2436 collects similar data on the outstanding volume of derivatives, but not on derivatives turnover. The Federal Reserve conducts both surveys in coordination with other central banks and forwards the aggregated data furnished by U.S. reporters to the Bank for International Settlements (BIS), which publishes global market statistics that are aggregations of national data. The estimated annual burden for this information collection is 2,100 hours.

Background and Justification

In January 1997, the Governors of the Central Banks of the Group of Ten Countries (G-10) approved a proposal by the Euro-currency Standing Committee (now called the Committee on the Global Financial System) to collect data on global derivatives activity from leading dealers, beginning at the end of June 1998. The Yoshikuni group, a working group of the Euro-currency Standing Committee, developed the reporting framework in a July 1996 report. The proposal outlined the derivatives market statistics that would be useful to central banks for oversight of global financial markets. They based the report design on the Common Minimum Framework that was developed and released jointly by the Basel Committee on Banking Supervision and the Technical Committee of the International Organization of Securities Commissions (IOSCO) in May 1995. The proposal also outlined the methodological considerations for collecting and aggregating these data. For example, the working group developed techniques to avoid double counting in the calculation of global market size statistics and fleshed out the level of detail required in data collection efforts.

The report design draws on the results of the April 1995 FR 3036. This survey was part of the first major coordinated effort by the G-10 central banks to collect data on global derivatives activity. The semiannual FR 2436 was designed to complement the triennial FR 3036, using the same format for reporting derivatives positions outstanding on both reports.

This procedure avoids duplication of effort for institutions participating in both data collections and improves the comparability of the data collected by the two reports. Furthermore, the Federal Reserve uses the FR 3036 data to monitor the growth of the derivatives activities at dealers not participating in the FR 2436 panel and to update the FR 2436 panel as necessary to maintain coverage of the vast majority of global derivatives activities.

Beginning in December 2004, the Federal Reserve began collecting data on credit default swaps as part of an international effort by the G-10 central banks. The rapid growth and size of the credit derivatives market increased the interest of the Federal Reserve and other central banks in comprehensive data on credit default swap activity.

The purpose of the FR 2436 is to obtain comprehensive and internationally consistent information on the size and structure of the OTC derivatives markets. The statistics are useful to the Federal Reserve, other central banks, and other parties who monitor patterns of activity in financial transactions. Due to the global nature of derivatives activity, only the cooperative efforts of central banks can generate the statistics required for effective monitoring of this activity. The Federal Reserve's involvement in this international reporting program, therefore, is necessary to ensure the availability of statistics needed for oversight of international financial markets. The FR 2436 provides comprehensive and consistent measures of global derivatives market size and participation not currently available from other sources.

Description of Information Collection

The panel of derivatives dealers provides data on outstanding positions (notional, gross positive and gross negative market values) with breakdowns by broad market risk category, product type, counterparty type, maturity, and specific underlying market risks—the currency, equity market, or reference entity that underlie the contract. In addition, reporters provide data on the gross market value of the entire portfolio, before and after netting.

Notional amounts outstanding (Tables 1A, 2A, 3A, 4A, 4B, 4C, and 5). A sum of notional amounts outstanding provides a means of approximating the scale and character of market transactions, in much the same manner as a sum of principal amounts provides for the cash market. Allocating notional amounts outstanding to market risk, instrument, maturity, and counterparty categories provides greater insight into the exposures to price risks transferred between contracting parties. Additionally, regularly published data on notional amounts enhance market transparency and permit market participants to compare, over time, the size and composition of their derivatives activities with those taking place in the market as a whole.

Gross positive and negative market values (Tables 1B, 1C, 2B, 2C, 3B, 3C, 4D, and 6). Gross market value figures show the magnitude of unsettled changes in value of derivatives contracts outstanding at the time of reporting. Semiannual reporting produces a series of changes in gross market value over time. Such a time series is a valuable source of information for researchers and market participants in developing an understanding of the role and function of derivatives markets in financial systems in various circumstances.

The 1995 global survey of derivatives markets found small net market value positions in derivatives for reporting U.S. dealers. The average net market value as a percentage of the total market value for foreign exchange and interest rate derivatives contracts with customers, foreign dealers, and non-reporting dealers was 1 percent. These positions were interpreted as showing that derivatives dealers had not taken large net exposures in meeting customer demands in derivatives. The availability of a time series of semiannual data on market values provides a means to better assess the risk intermediation services that are being offered by dealers as a group.

Furthermore, gross market values can be used as one measure of market size; they show, at a given point in time, the amount of risk that is transferred using derivatives contracts. Although, this measure requires summing the gross positive market values of *all* market participants (not just of reporters), the gross positive market value of non-reporting firms can be captured by measuring the negative market value of reporting firms' contracts with non-reporting firms. Thus, market size statistics based on gross market value can be constructed while maintaining a limited reporting population.

Additional detail. The FR 2436 collects further detail on the notional amounts and gross positive and negative market values of outstanding derivatives contracts.

Broad market risk categories: Foreign exchange rate, gold price, interest rate, equity, commodity, and credit.

Product types: Forward contracts, swaps, and bought and sold OTC options. Credit derivatives data are collected on only one type of product, credit default swaps, which are broken out into single-name and multiple-name instruments.

Counterparty types: Reporting dealers, other financial institutions, and non-reporting financial institutions. For credit default swaps, other financial institutions are further broken out into (1) banks and securities firms, (2) insurance, reinsurance, and financial guaranty firms, and (3) other. This finer disaggregation of counterparty types gives central banks and other data users a clearer picture of how credit default swaps transfer credit risk within the global financial system.

Remaining maturities: One year or less, over one year through five years, and over five years.

Underlying market risks: Data for foreign exchange and single-currency interest rate contracts are reported by currency for each G-10 currency, as well as for any additional currency for which a material amount of contracts is outstanding. Two currencies are reported for each foreign exchange contract. Data on equity derivatives are reported in six categories according to the region of the referenced equity market: U.S., Japanese, European (excluding emerging markets in Eastern Europe), Latin American, Other Asian, and Other. Data on the notional amounts of credit default swaps are reported by characteristics of the reference entity: whether it is a sovereign or not, and whether its credit rating is investment grade or sub-investment grade or it is unrated.

Protection bought and sold: For credit default swaps, data are reported according to whether the contract buys or sells credit protection. Distinguishing between protection bought and protection sold is of interest because it gives some indication of how credit default swaps are used to shift credit risk among market participants.

Reporting Panel

The reporting panel, together with reporters from other reporting countries, represents approximately 90 percent of total global activity in each of the major categories of derivatives. U.S. firms were invited to report the FR 2436 based on the size of their derivatives positions reported in the April 1995 triennial derivatives market survey, and twelve firms agreed to report the FR 2436 beginning in 1998. Since 1998, mergers and acquisitions among reporting firms have reduced the original twelve reporters to six firms. The panel is periodically reviewed, based on the results of the FR 2436 and FR 3036 surveys, supplemented with data from the FR Y-9C and 10-K reports. In 2003, one additional U.S. firm agreed to join the reporting panel. Currently, seven U.S. institutions voluntarily report the FR 2436.

Frequency

Respondents file the FR 2436 semiannually, as of the close of business each June 30 and December 31.

Time Schedule for Information Collection and Publication

Data are submitted to the Federal Reserve Bank of New York (FRBNY) within seventy-five days of the as-of dates, June 30 and December 31 each year. After editing the data, FRBNY sends the aggregated data to the BIS and sends reporter-level and aggregated data to the Board. The Federal Reserve uses the reporter-level data to compute aggregated concentration statistics, which it sends to the BIS. The BIS compiles the aggregated data and the concentration statistics from U.S. institutions with those from the approximately fifty additional reporters from other G-10 countries and constructs and publishes global derivatives market statistics. Data from the reporting securities firms can be shared with the Securities and Exchange Commission.

Legal Status

The Board's Legal Division has determined that this report is authorized by law [12 U.S.C. '' 225a, 263, 348a, and 353-359] and is voluntary. Individual respondent data are regarded as confidential under the Freedom of Information Act [5 U.S.C. '552(b)(4)].

Consultation Outside the Agency

The Federal Reserve consulted with other G-10 central banks on the details of the data to be collected. On July 23, 2007, the Federal Reserve published a notice in the *Federal Register* (72 FR 40152) requesting public comment for sixty days on the extension, without revision, of the Semiannual Report of Derivatives Activity. The comment period for this notice expired on September 21, 2007. The Federal Reserve received no comments. On October 17, 2007, the Federal Reserve published a final notice in the *Federal Register* (72 FR 58851).

Estimate of Respondent Burden

The total annual burden for this report is estimated to be 2,100 hours, as shown in the table below. Seven U.S. institutions report semiannually and take an average of 150 hours per response. This represents less than 1 percent of total Federal Reserve burden for all reports.

	Number of respondents	*Annual frequency*	*Estimated average hours per response*	*Estimated annual burden hours*
FR 2436	7	2	150	2,100

The total cost to the public is estimated to be $118,650.[1]

Sensitive Questions

This collection of information contains no questions of a sensitive nature, as defined by OMB guidelines.

Estimate of Cost to the Federal Reserve System

The cost of collecting and processing the data is absorbed by the Regulatory Reports Division of the FRBNY. The current cost associated with the FR 2436 is $100,000 per year.

1 Total cost to the public was estimated using the following formula. Percent of staff time, multiplied by annual burden hours, multiplied by hourly rate: 10% - Clerical @ $25, 80% - Managerial or Technical @ $55, and 10% - Senior Management @ $100. Hourly rate estimates for each occupational group are averages using data from the Bureau of Labor and Statistics, *Occupational Employment and Wages*, news release.