Commodity Futures Trading Commission
Office of Public Affairs
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
www.cftc.gov

Q & A – Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants

What is the goal of the rulemaking?

The Dodd-Frank Act authorizes the Commission to adopt regulations setting forth standards for the timely and accurate confirmation, processing, netting, documentation, and valuation of swaps. The goal of the final rules is to establish standards for accurate swap trading relationship documentation, including documentation concerning the use of the end-user clearing exception, as well as requirements for swap confirmation, portfolio reconciliation, and portfolio compression.

What registrants are covered by the final rules?

The final rules apply to swap dealers and major swap participants.

Were comments from the public received on the final rules?

Yes. The Commission received a total of approximately 62 comment letters directed specifically at the proposed rules. The Commission considered each of these comments in formulating the final rules.

What are the trading relationship documentation requirements?

The final rules require swap dealers and major swap participants to document all terms governing their trading relationship in writing, including terms related to credit support arrangements and swap valuation methodologies. The final rules also require swap dealers and major swap participants to document certain information related to clearing of their swaps and, if applicable, a counterparty's reliance on the end user exception to clearing.

What are the end user exception documentation requirements?

The final rules require swap dealers and major swap participants to document certain information relating to the qualifications of counterparties who invoke the end-user clearing exception.

Documentation must include: (1) the identity of the counterparty; (2) that the counterparty has elected not to clear a particular swap; (3) that the counterparty is a non-financial entity; (4) that the counterparty is hedging or mitigating a commercial risk; and (5) that the counterparty generally meets its financial obligations associated with non-cleared swaps. Certain of that documentation need not be obtained by the swap dealer or major swap participant, under certain circumstances.

What are the confirmation requirements?

With respect to swap transactions with a person who is a swap dealer or major swap participant, the final rules require each swap dealer and major swap participant to execute a confirmation for the swap transaction as soon as technologically practicable, but no later than the time periods set forth in the rule.

With respect to swap transactions with a person who is not a swap dealer or major swap participant, the final rules require each swap dealer and major swap participant to send an acknowledgment of the transaction as soon as technologically practicable, but no later than the time periods set forth in the rule. For each such transaction, the swap dealer or major swap participant must establish, maintain, and follow written policies and procedures reasonably designed to ensure that it executes a confirmation as soon as technologically practicable, but no later than the time periods set forth in the rule.

The procedures must include an obligation to furnish to, or receive from, its prospective counterparty, upon request, a draft acknowledgement specifying the terms of the swap transaction (other than pricing and the terms to be definitively agreed to at execution), prior to execution.

The confirmation requirements do not apply to swap transactions: (1) executed on a swap execution facility or designated contract market, provided that the rules of the swap execution facility or designated contract market establish that confirmation of all terms of the transaction shall take place at the same time as execution; or (2) submitted for clearing by a derivatives clearing organization, provided that (i) the transaction is submitted for clearing as soon as technologically practicable, but no later than the times set forth in the rule, and (ii) confirmation of all terms of the transaction takes place at the same time as the transaction is accepted for clearing.

While the Commission encourages the use of master confirmation agreements and other standardized documentation that has been developed by the industry, the final rules do not prescribe the particular acknowledgement or confirmation documentation that market participants are required to use, nor does it prescribe a particular venue or platform for confirmation.

What are the portfolio reconciliation requirements?

The portfolio reconciliation requirements only apply to swap transactions that are not cleared by a derivatives clearing organization.

Swap dealers and major swap participants must reconcile swap portfolios with other swap dealers or major swap participants with varying frequency, depending upon the size of the particular portfolio. Discrepancies in material terms identified as part of a portfolio reconciliation process must be resolved immediately.

Swap dealers and major swap participants must establish, maintain and follow written policies and procedures reasonably designed to resolve any valuation discrepancy (of 10% or greater) as soon as possible, but no later than five business days. The policies and procedures also must identify how the swap dealer or major swap participant will comply with any variation margin requirements under section 4s(e) of the CEA and Commission regulations pending resolution of such discrepancy.

The final rules do not prescribe any specific procedures that must be followed to resolve a discrepancy in valuation.

For swap portfolios involving a counterparty that is not a swap dealer or major swap participant, the final rules require that swap dealers and major swap participants must establish written policies and procedures to perform portfolio reconciliation with varying frequency, depending upon the size of the portfolio. Swap dealers and major swap participants also are required to establish written procedures reasonably designed to resolve any identified discrepancies in the material terms or valuation of swaps in a timely fashion.

Swap dealers and major swap participants must notify the Commission and any applicable prudential regulator (and the Securities and Exchange Commission, for security-based swaps) of any swap valuation dispute in excess of $20,000,000 (or its equivalent in any other currency) if not resolved within: (1) 3 business days, if the dispute is with a counterparty that is a swap dealer or major swap participant; or (2) 5 business days, if the dispute is with a counterparty that is not a swap dealer or major swap participant.

What are the portfolio compression requirements?

With respect to portfolios among swap dealers and major swap participants, each swap dealer and major swap participant must establish, maintain, and follow written policies and procedures for: (1) terminating each fully offsetting swap in a timely fashion, when appropriate; (2) periodically engaging in bilateral portfolio compression exercises, when appropriate; and (3) periodically engaging in multilateral portfolio compression exercises, when appropriate.

The final rules do not mandate portfolio compression exercises for swaps between a swap dealer or a major swap participant and other types of counterparties. Instead, swap dealers and major swap participants must establish, maintain, and follow written policies and procedures for periodically terminating fully offsetting swaps and for engaging in portfolio compression exercises, to the extent requested by the counterparty.

The portfolio compression requirements and related recordkeeping obligations do not apply to swaps cleared by a derivatives clearing organization.