



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5977
Facsimile: (202) 418-5407
gbarnett@cftc.gov

Division of Swap Dealer and
Intermediary Oversight

Gary Barnett
Director

CFTC Letter No. 13-31
No-Action
June 26, 2013
Division of Swap Dealer and Intermediary Oversight

Robert G. Pickel
Chief Executive Officer
International Swaps and Derivatives Association, Inc. ("ISDA")
360 Madison Avenue, 16th floor
New York, NY 10017

Re: No-action relief as to the "material terms" of a swap for purposes of portfolio reconciliation

Dear Mr. Pickel:

This letter is in response to your request on behalf of your members and other similarly situated swap dealers ("SDs") and major swap participants ("MSPs") with obligations to engage in portfolio reconciliation under Commission Regulation ("Regulation") 23.502¹ (collectively, "Transaction Counterparties"), in which you seek an interpretative letter from the Division of Swap Dealer and Intermediary Oversight ("Division") of the Commodity Futures Trading Commission (the "Commission") regarding what terms constitute the "materials terms" of a swap.

Regulation 23.502 requires SDs and MSPs to reconcile their swap portfolios with one another and provide counterparties who are not registered as SDs and MSPs with regular opportunities for portfolio reconciliation.² Regulation 23.500(i) defines the term, "portfolio reconciliation," as "any process by which the two parties to one or more swaps: (1) Exchange the terms of all swaps in the swap portfolio between the counterparties; (2) Exchange each counterparty's valuation of each swap in the swap portfolio between the counterparties as of the close of business on the immediately preceding business day; and (3) Resolve any discrepancy in

¹ 17 C.F.R. § 23.502.

² *Id.*; see *Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants*, 77 Fed. Reg. 55,904, 55,926 (Sept. 11, 2012) (hereinafter, "Portfolio Reconciliation Final Rule").

material terms and valuations.”³ Regulation 23.500(g) defines “material terms” to mean “all terms of a swap required to be reported in accordance with part 45 of this chapter.”⁴

The Commission also has described portfolio reconciliation, generally, as follows:

“Portfolio reconciliation is a post-execution processing and risk management technique that is designated to (i) identify and resolve discrepancies between the counterparties with regard to the terms of a swap either immediately after execution or during the life of the swap; (ii) ensure effective confirmation of terms of the swap; and (iii) identify and resolve discrepancies between the counterparties regarding the valuation of the swap.”⁵

Regulation 23.502, which requires that swap counterparties engage in portfolio reconciliation (or provide opportunities for portfolio reconciliation) at regular intervals, was promulgated pursuant to sections 4s(h) and 4s(i) of the Commodity Exchange Act (“CEA”),⁶ as added by section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,⁷ which, among other things, directed the Commission to prescribe regulations for the timely and accurate confirmation, processing, netting, documentation and valuation of all swaps entered into by SDs and MSPs.⁸ Regulation 23.502 derives from the understanding that “[b]y identifying and managing mismatches in key economic terms and valuation for individual transactions across an entire portfolio . . . overall risk can be identified and reduced.”⁹

You are seeking guidance that certain data elements may be excluded from portfolio reconciliation required under Regulation 23.502. Specifically, you request that the following data fields (“Excluded Data Fields”) shall not be considered “material terms” of a swap for purposes of Regulation 23.502:

1. An indication that the swap will be allocated;
2. If the swap will be allocated, or is a post-allocation swap, the Legal Entity Identifier of the agent;
3. An indication that the swap is a post-allocation swap;
4. If the swap is a post-allocation swap, the unique swap identifier;
5. Block trade indicator;
6. Execution timestamp;
7. Timestamp for submission to swap data repository;

³ 17 C.F.R. § 23.500(i); *see Portfolio Reconciliation Final Rule*, 77 Fed. Reg. at 55,926.

⁴ 17 C.F.R. § 23.500(g).

⁵ *Portfolio Reconciliation Final Rule*, 77 Fed. Reg. at 55,926.

⁶ 7 U.S.C. §§ 6s(h)-(i).

⁷ Pub. L. No. 111-203, 124 Stat. 1376 (2010).

⁸ *Portfolio Reconciliation Final Rule*, 77 Fed. Reg. at 55,926 (“[P]ortfolio reconciliation involves both confirmation and valuation and serves as a mechanism to ensure accurate documentation.”).

⁹ *Id.*

8. Clearing indicator;
9. Clearing venue;
10. If the swap will not be cleared, an indication of whether the clearing requirement exception in CEA section 2(h)(7) has been elected;
11. The identity of the counterparty electing the clearing requirement exception in CEA section 2(h)(7).

You are likewise requesting that the Division interpret the reference to “the terms” of a swap transaction in clause (1) of Regulation 23.500(i) for the definition of “portfolio reconciliation” as referring to the “material terms” of a swap other than the Excluded Data Fields.

You contend that your requested interpretation of “material terms” (*i.e.*, as not including the Excluded Data Fields) would facilitate portfolio reconciliation by allowing market participants to focus on exchanging and reconciling information relevant to the ongoing valuation of their swaps portfolios, and avoid unnecessary costs and complexity associated with the reconciliation process. Accordingly, you believe that the requested interpretation is consistent with the policy objectives of Regulation 23.502.

Staff Position

Regulation 23.502 is designed to facilitate consistent valuations of swap portfolios among counterparties and to promote sound risk management by requiring counterparties to engage on an ongoing basis in portfolio reconciliation. Achieving these goals requires that counterparties periodically compare, confirm, and where necessary, reconcile the terms that primarily determine each swap’s value on an ongoing basis.

After considering your requests, the Division has determined to provide no-action relief.¹⁰ The Division will not recommend an enforcement action against an SD or MSP that omits the Excluded Data Fields from the portfolio reconciliation process required under Regulation 23.502.

This letter, and the positions taken herein, represent the view of this Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse Transaction Counterparties from compliance with any other applicable requirements contained in the Act or in the Regulations issued thereunder. For example, the Transaction Counterparties remain subject to all antifraud provisions of the Act.¹¹ Further, this letter, and the relief contained herein, is based upon the representations made to the Division. Any different, changed or omitted material facts or circumstances might render this letter void.

¹⁰ ISDA requested that the Division issue an interpretative letter. The Division has determined instead to provide no-action relief.

¹¹ See, *e.g.*, sections 4b and 4o of the Act. 7 U.S.C. §§ 6b & 6o.

Mr. Pickel
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Should you have any questions, please do not hesitate to contact me at (202) 418-5977, or Gregory Scopino, an attorney on my staff, at (202) 418-5175.

Very truly yours,

Gary Barnett
Director
Division of Swap Dealer and Intermediary Oversight

cc: Regina Thoele, Compliance
National Futures Association, Chicago

Jamila A. Piracci, OTC Derivatives
National Futures Association, New York