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**Chairs:** Michael Clarke ([michael-c.clarke@ubs.com](mailto:michael-c.clarke@ubs.com)), Shaun Sheppard ([shaun.sheppard@gs.com](mailto:shaun.sheppard@gs.com))

**ISDA policy lead:** Nichole Framularo ([nframularo@isda.org](mailto:nframularo@isda.org))

### Questions Submitted in Writing for the Q&A Session:

1. Timing: as we have previously intimated, in our view, the proposed timelines put enormous time pressures on Front Office staff to check deals and speak with the other institution - given markets we are concerned that this will prove unlikely to work inside the timelines on a number of occasions - so what happens then ?

*A: The approach for timing in the DR protocol was to start out with the shortest timelines so that in the event of a credit crisis, parties are not impeded to issue notices of default, etc. Therefore, the Standard Timings as listed in the DR protocol are very tight, which is the situation you would want in a credit crisis situation. However parties have the option to extend the timelines or even further accelerate the timings as needed for the various situations. The DR protocol also contains Extended Timings which have slightly longer timelines and in the ordinary course of business is the option parties are expected to elect.*

*With respect to the consequences if a party were to miss the timelines in the DR protocol for any step, this still requires further work. As drafted if a party fails to perform the actions required then they would 'lose' the dispute and must move collateral based on the other party's call. However depending on the final implementation of the DR protocol this may change.*

2. Values for complex trades: this is a tricky issue. We understand that some market participants take risk reserves at a portfolio level so their mid price for collateral purposes is likely to differ from their unwind price. So we will always have a difference. How should this be addressed?

*A: Generally, firms take risk reserves for 2 reasons. One, in order to make a correction / adjustment that would bring the trades in the portfolio closer to fair market value. If that were the case, then the reserve needs to be allocated at the trade level so that the mid market price can be used for collateral purposes. If this is not done, then margin disputes can arise as a result.*

*A second reason for taking a provision at the portfolio level could be to reflect internal liquidity reserves or other firm-specific reasons. Generally these reserves express a specific firm view and would not be relevant to establishing fair market value.*

3. The results obtained through the mechanism will continue to be used for the purpose of computing margin calls until such time as the relevant markets move or additional transparency of fair value develops ("**Longevity of results**" in 6.6). In normal circumstances, the value of exposures will change according to the market movement on daily basis, so is it correct to understand that the longevity of the results is one day? In response to the Q2 of 11.5

([http://www.isda.org/uploadfiles/docs/ISDA\\_DR\\_Phase\\_1\\_Commentary\\_Received\\_For\\_Review.doc](http://www.isda.org/uploadfiles/docs/ISDA_DR_Phase_1_Commentary_Received_For_Review.doc)) explains the value can be used for one day (Therefore, essentially the dealer poll result (value of the trade) can only be used for 1 day...), and this will be applied for 6.6 i) as well?

*A: For markets that move continuously, the Longevity would be short, but for the markets where there is infrequent price availability, the language "as the relevant markets move or additional transparency of fair value develops" is designed to allow the parties to continue to use a DR result for a period of time, until one or both parties feel that new information is available to support a re-marking of the position. Note that there is a maximum Longevity which varies depending on the method that is used. This avoids undergoing the entire process on a daily basis.*

4. When an Intractable Dispute occurred, each party need to notify its primary regulatory supervising agency within 30 days of the dispute originally arising ("**Intractable Dispute Disclosure**" in 6.5). In what purposes should the intractable dispute be reported to the regulators? The reason behind this question is that it should be clarified in order to know what department of Japanese FSA (in case of Japanese firms) should they need to report to.

*A: See Question 10*

5. The quote provided by the clearinghouse is granted the highest priority and effectively trumps all other types of quotes. (6.4(iv), footnote 23 on page 16): I would like to know why this treatment is considered appropriate. I suppose this is because valuation by clearinghouses are used for settlement of many trades. But clearinghouses are accustomed only to fairly standardized trades, whereas trades where margin disputes arise are usually exotic trades that clearinghouses are ill-equipped to cope with. So I am concerned that the trust on clearinghouse pricing here might be misplaced. Clearing Houses are not supposed to provide prices for complex trades that they do not clear, why would we ask for a Clearing House price on those trades?

*A: The intention isn't to ask the Clearing House to price a trade, but to affirmatively state that if a trade is traded on a Clearing House, then the Clearing House price is final; the rationale being that Clearing Houses should see the greatest volume and be the best price source. However, it is unlikely that more complex trades would have a Clearing House price.*

6. It seems that the exposure calculated in step 4b is supposed to be effective for some period (6.6). But as such exposure fluctuates day by day, many market participants may find this treatment hard to endorse. Or this wording says "until such time as the relevant market move or..." so this itself imply that the longevity of the result of step 4b is only 1 day. Similar view is expressed in the response to 11.5 Q2 in page 18 of 25 in the attached link

[http://www.isda.org/uploadfiles/docs/ISDA\\_DR\\_Phase\\_1\\_Commentary\\_Received\\_For\\_Review.doc](http://www.isda.org/uploadfiles/docs/ISDA_DR_Phase_1_Commentary_Received_For_Review.doc)

Does this view (longevity is basically only for 1 day) continue to be the basic understanding?

*A: See Question 3*

7. If parties, after exhausting process 4b, still fail to resolve a dispute, then they "shall be obliged to report" to the relevant authority (6.5). I would like to know what is the point of doing this. (If this point is unclear, we cannot be sure to which section of the relevant authority we should report).

*A: See Question 10*

8. Question related to section 6.4 (c) (ii):

The presumption that the firm quote from a dealer establishes a market price for the transaction in dispute seems to assume that the dealer is actually putting itself at real economic risk that some third party will actually hit its bid or offer price. Is this assumption warranted where the dealer is itself in financial distress? Would anyone enter into a trade with Bear Stearns or Lehman Brothers in the days leading up to their demise simply because they published an attractive quote on a transaction? If not, why should the firm dealer quote be given any higher weight in this situation than the end-user's valuation?

*A: See Question 20*

### **Questions raised during the Q&A Session:**

9: In regard to the language for one side to accelerate the process. What was the thinking there? Why would one side be able to accelerate?

*A: The rationale for allowing the acceleration to be unilaterally invoked is basically to allow a non defaulting party in a credit event situation the ability to accelerate, or to prevent a party from using the DR protocol to delay collateral movement. For example:*

- *Protect the non defaulting party: Where two parties have mutually elected to use Extended Timings, but before the DR process was completed one of the parties was facing an imminent credit event, the other party should be able to accelerate the process up to Step 4b (Formal dispute resolution).*
- *Prevent parties from using the DR protocol to delay collateral movement: If one party invoked the Dispute Resolution process simply to try and delay the process, the other party can accelerate to Step 4b*

*It should be noted that acceleration can take place up to Step 4b only, where upon the parties must undergo Formal Dispute Resolution (Market Poll)*

10: Part 4(b): What is the purpose of notifying regulators? Are we expecting regulators to intervene and help resolve the dispute?

*A: Currently this is just a placeholder as it is more appropriate for the regulators to tell us what they expect than vice versa. However it has been agreed in principle that there will be a level of reporting to the regulators. The regulatory community is expected to revert back with the types of information they expect to see. Initial discussions indicate the reporting will be related to disputes entering Step 4a, 4b, Intractable disputes, disputes exceeding certain criteria (e.g. 30 days old, dispute amount greater than x, etc.).*

*There is no formal process agreed or established yet on how the regulators will treat the information they receive. However it could range from simply serving as an early warning to prompting an intervention by the regulators to mediate between the two parties, especially if the dispute amount is significant.*

11: Could you please share the detail about which regulators you've been in dialog with?

*A: The NY Fed have been our main point of contact who are in regular discussions with other regulators globally. The Dispute Resolution Drafting team (consisting of 5 buy and 5 sell side reps) recently had a discussion with the regulators regarding Dispute Resolution. Regulatory representatives included BaFin, Commission Bancaire, Swiss FINMA, UK FSA, Japan FSA, CT Department of banking, FDIC, FR Board, FRBNY, FR Richmond, NYSBD, OCC, SEC*

12: Implementation: Do we envision having templates to standardize communication between ourselves for the different steps of the DR process (i.e. communicate transactions under investigation, under dispute resolution, etc.) and various options available (i.e. acceleration, extended timings, etc.) that could remove ambiguity?

*A: This will be more formally addressed as part of the implementation plan, but templates could be part of that solution. Another suggestion that has been informally raised is the idea of potentially having a central infrastructure for the tracking, reporting, and implementation of the Dispute Resolution process. If this turned out to be desirable we would look to issue an RFP.*

13: Will there be any specific rules taking into account the potential provisions for market risk in the market poll mechanism?

*A: Market poll quotes are expected to be given without credit factors in the pricing. However this is a topic that requires further review by the drafting team; the speaker is encouraged to include this as one of the items submitted during the comment period for consideration.*

14: Even though the document states that trades with differences within the tolerance levels can be deemed as Transactions Under investigation, can the Dispute Resolution still be invoked if there was no portfolio level collateral dispute or do both parties have to declare that they are formally in a dispute?

*A: If a party believes there are disputes with the underlying trades, they can invoke the DR process even if the entire call amount is agreed (e.g. the Undisputed Collateral Amount is equal to the full amount of the margin call). The DR protocol can be applied to the trades in question in order to resolve the trade level disputes.*

15: Is it intended that this will have legal effect across all parties and how will parties sign-up?

*A: This is an implementation question that is still open. The original intent was to issue this as a binding protocol for firms to adhere to which would amend all bilateral contracts of the adhering parties.*

*However, the Phase 1 comments that were provided indicated an emerging consensus that there was a strong desire to issue the Dispute Resolution protocol as a Best Practice. This is mainly due to concerns about using a legal document that hasn't been thoroughly tested in the market yet. After discussion with the regulators, they have indicated that this will eventually need to be a legally binding implementation. But they are not opposed to the idea of a phased implementation where the rollout could start as a Best Practices endorsed by ISDA and/or regulators and eventually become a binding protocol. How this will work is an open item that needs to be addressed before September.*

16: Could you please review the timeline and key milestones for Dispute Resolution?

*A: August 7: Public Commentary period for Phase 2 (version 2) of the Dispute Resolution ends. All comments should be submitted to ISDA.*

*September 30: Final version of the Dispute Resolution document plus an implementation plan submitted to the Fed*

*Key activities between now and the end of September:*

- Implementation Planning: Including timelines and specifics if we are proposing a phased rollout (e.g. Fed 15 and large HF first, rollout as a best practice by XXX and legally binding protocol by XXX)*
- Industry Infrastructure requirements*
- Backtesting: Apply past and example dispute scenarios with the current process to identify any pitfalls or issues not addressed*

17: Could you give us the background behind developing the proposal?

*A: Many firms observed in 2008 that the dispute resolution language in the CSA did not necessarily work under all circumstances. Also, the current Dealer Poll mechanism was inefficient and in most cases did not yield a result. The dispute resolution work to revise the process looks to address those issues and to improve on the overall dispute resolution process. For example, the new Dispute Resolution proposal looks to better define what is meant by 'Market Quotation', introduces the concept of 'longevity' to avoid repeating the dispute resolution process daily where it isn't necessary, etc. Basically, the new dispute resolution process aims to increase the likelihood that a dispute will be resolved and margin calls will be agreed.*

18: Do you think there will be a high risk of cherry picking?

*A: The intention is to promote more transparency in pricing via a community self-help mechanism. The principles underlying the market polling mechanism a) work on the basis that two-way firm executable prices take precedence over any other prices (e.g. indicatives) and b) create an obligation that any firm that holds themselves out to be a Reference Market Maker, if called upon to provide a quote, will provide this information. This is a fundamental change from the current mechanism.*

19: Following on from question 18: Footnote 18 doesn't seem like a very strong sanction for declining to give a quote as a Reference Market Maker. Is there a more substantive consequence?

*A: That specific footnote is related to the responsibility of a Market Making Party who is one of the disputing parties. There are 2 different responsibilities that a Reference Market Maker is expected to carry out in the new proposal:*

- 1- If the party is one of the Disputing Parties: To qualify as a Market Making Party in the Dispute Resolution process, the firm must provide a 2-way firm executable quote. If the party does not provide such quote, they will be deemed a Rebutting party and will follow the Dispute Resolution process as a Rebutting Party (Relates to Footnote 18)*
- 2- If the party is not one of the Disputing Parties: Firms who are Reference Market Makers must provide Reference Quotes if approached and if they are able to. The Reference Quotes provided will be used for the Market Poll to resolve the dispute between the disputing parties (Relates to Footnote 22). This is the 'community self-help' mechanism discussed in Question 18.*

20: 6.4(iv)(c)(ii): What happens if the Dealer is in a credit distress situation (similar to Lehman/Bear), when no one would step in?

*A: This is one of the items that does not have an easy solution and continues to be a key item the Dispute Resolution Drafting team is discussing. There may be no entirely satisfactory answer.*

21: All Reference Market Makers are expected to provide quotes. If they don't, is there any consequence or is it a good faith statement?

*A: It is essentially on a good faith basis. The possible solutions would be to escalate within the non complying firm, escalate to the regulators, or file a lawsuit. None of the above would provide a timely answer or guarantee an answer so the rationale is to incentivize firms to provide Reference Quotes as the expectation is all firms will need this service at some point.*

22: How does this work together with the CSA?

*A: The implementation discussion will determine how the new Dispute Resolution process will 'slot' into the current CSA. The key is to establish and agree how and which sections of the CSA should be replaced so that one does not end up back at the beginning of the dispute resolution paragraph (4 or 5 in the CSA) with no resolution and be forced to undergo the current process again.*

23: If the dispute remains under the protocol, will you still be able to terminate under the CSA?

*A: Yes, those aspects of the CSA remain unchanged and should work as it currently does.*

24: Is the intention that this process will be used for other types of dispute (i.e. terminations)?

*A: No, the intention is to resolve margin disputes between the two disputing parties.*

25: If under the new DR proposal, a result was produced but the disputing party fails to deliver the collateral what can the other party do?

*A: Under the CSA, that would be a failure to deliver collateral and you could issue a notice of default. There is no intention to change that part of the CSA. The new DR Proposal leads the disputing parties through the administrative steps of trying to resolve the disputes. It should be noted however that parties can also ultimately agree to disagree and deem the dispute as Intractable. In which case there will likely be reporting to the regulators, additional reg cap amounts, etc.*