

Asia Pacific Collateralised Portfolio Reconciliation Memorandum of Understanding

03 January, 2011

Introduction

Significant growth in the derivatives market opens up the potential for operational risk if parties involved, for one reason or another, are not accurately reflecting derivative transactions in their system records. In addition there are growing regulatory requirements to validate the accuracy of derivative portfolio populations.

Portfolio reconciliation was established as a process to verify the accuracy of a firm's trade population using live system data by comparing the two counterparty's records of a bi-lateral OTC portfolio as of a given business date. A particular use of the reconciliation process has been taken up by the collateral function, on a reactive basis to investigate and identify trades giving rise to a collateral dispute, and on a pro-active basis to ensure bi-lateral portfolios remain in line to mitigate the potential for disputes arising.

The objective of collateralised portfolio reconciliation is to ensure that two organisations have one consistent record for a defined portfolio (or group of portfolios) by comparing the portfolio contents provided by each participant in order to individually match the underlying trades. The reconciliation process uses a minimum set of fields necessary to ensure accurate matching and, as standard practice, includes the mark-to-market value each party has assigned to each trade.

The 14 major dealers in the OTC derivatives market (each a **Major Dealer**) have set out a comprehensive set of commitments to reform market practice in the collateral management space in their letters to certain regulators which include the commitment to put in place robust portfolio reconciliation practice to detect significant trade population and valuation differences that could give rise to disputed collateral calls (the **global regulatory commitment**).

The industry would like to promote regular collateralised portfolio reconciliation in the Asia Pacific region on a voluntary basis. Under the auspice of ISDA Collateral Steering Committee, ISDA Asia Pacific Collateral Management Operations Working Group drafted this Memorandum of Understanding (**MoU**) which is designed for adoption between two members in the Asia Pacific region who are not subject to the global regulatory commitment (each a **non-Major Dealer**). The MoU may also apply to collateralised portfolio reconciliation between a non-Major Dealer and a Major Dealer to the extent that it does not conflict with the global regulatory commitment applicable to the Major Dealer. The standards set out in this MoU were tested in two pilot runs earlier which generated satisfactory results.

The scope of this document is limited to reconciliations performed as part of the OTC collateral function, and applies only to portfolios governed by a bi-lateral ISDA Credit Support Annex (CSA), Credit Support Deed (CSD) or other OTC collateral agreement.

When carrying out portfolio reconciliations, adherence parties of this MoU are recommended to refer to the ISDA Portfolio Reconciliation Best Practices and Minimum Market Standards published on January 20, 2010, as may be amended and supplemented from time to time.

Objectives of MoU

1. Reduce operational risk by identifying mismatches in a timely manner through regular trade reconciliation; and
2. Increase efficiencies in the implementation of OTC collateral agreements.

This MoU does not, in and of itself, create any legally binding or enforceable obligations on the part of any party which adheres to the MoU.

Adherence to the MoU

A firm may adhere to this MoU by completing and delivering an email to isdaap@isda.org substantially in the form of Exhibit 1 to this MoU (an Adherence Email) to ISDA.

Eligibility

To be eligible for this initiative, a firm should satisfy the following criteria:

1. having business operations in the Asia Pacific region;
2. having executed at least one bi-lateral OTC collateral agreement (such as ISDA CSA, CSD or other OTC collateral agreement); and
3. having staff dedicated to carrying out collateralised portfolio reconciliation as prescribed in this MoU on a continuous basis.

Mechanism

For firms adhering to this MoU, they are expected to perform a weekly (or on a more frequent basis as they may bilaterally agree to) reconciliation with Designated Counterparties. The process consists of exchanging their Trade Portfolios with the same Valuation Cut-Off Date between the parties on the Portfolio Exchange Date.

Firms are expected to reconcile the file contents as soon as possible and clarify with their in-house colleagues or Designated Counterparties to solve any discrepancy located in the trade reconciliation process.

There is no restriction on the reconciliation approach. Firms may carry out reconciliation using automated solutions provided by a vendor, in-house solutions or spread sheet. It was noted in the pilot run earlier that the time spent on reconciliation using automated solutions was shorter than the time spent using other approaches, therefore, firms are encouraged to use automated solutions.

Firms should inform their Designated Counterparties as soon as possible when there is any disruption to the reconciliation.

Firms should inform their Designated Counterparties as soon as possible if their contact lists for portfolio reconciliation are different from the contact lists for daily collateral management.

Data to be provided and reconciled in the Trade Portfolio

Below are the minimum standards for data that are required for each trade in the Trade Portfolio. Firms are encouraged to provide more details of a trade to achieve higher accuracy.

1. Firm Name

The name of your booking entity (which can be in abbreviation as long as it is recognizable by your Designated Counterparty).

2. Counterparty Name

The name of your counterparty (which can be in abbreviation as long as it is recognizable by your Designated Counterparty).

3. Trade Identification

Your trade ID (if applicable) in the Confirmation together with any common market IDs (if available) that may have been assigned by an electronic confirmation platform. For avoidance of doubt, Trade Identification is not a matching field.

4. Trade notional and currency

Trade notional and its currency. Firms are recommended to use the first notional if a trade has more than one notional during the life of the trade. For any trade which has been partially unwound, firms are recommended to use the latest notional after the unwind. For any dual currency trade, firms are recommended to include both notional and the names of the currencies.

5. Trade date and maturity date

6. MTM valuation calculated by the sending firm, valuation currency and valuation date. For avoidance of doubt, these are not matching fields.

Definitions

“Designated Counterparties” means the counterparties that you have selected from the list of the entities that have adhered to this MoU and agreed to reconcile their portfolios with you. The counterparties that you have selected should have a scalable number of trades in the Trade Portfolio which is recommended to be 1000 trades. Parties are free to agree to a lower threshold. The number of Designated Counterparties that you should select is recommended to be at least three within the first three months of your adherence to the MoU and be gradually increased over times.

“Portfolio Exchange Date” means a day on which you and your Designated Counterparty exchange the Trade Portfolio which is usually every Tuesday or a date agreed by the parties.

“Trade Portfolio” means the portfolio containing the trades governed by the collateral agreement between you and your Designated Counterparty.

“Valuation Cut-Off Date” means the day on which the file about your Trade Portfolio is produced which is usually every Monday or a date agreed by the parties.

Appendix

Please find the attached links to the following publications:

1. [Portfolio Reconciliation - Best Operational Practices dated November 30, 2011](#)
2. [Minimum Market Standards Standardised Data for Collateralized Portfolio Reconciliations – dated October 19, 2011](#)
3. [ISDA Portfolio Reconciliation in Practice Papers published in August, 2008](#)

EXHIBIT 1

Form of Adherence Email

Send to: isdaap@isda.org

Dear Sirs,

Asia Pacific Collateralised Portfolio Reconciliation Memorandum of Understanding - Adherence

The purpose of this letter is to confirm our adherence to the ISDA Asia Pacific Collateralised Portfolio Reconciliation Memorandum of Understanding as published by the International Swaps and Derivatives Association, Inc. on 03January 2011 (the MoU). This letter constitutes an Adherence Email as referred to in the MoU. The definitions and provisions contained in the MoU are incorporated into this Adherence Email.

We hereby appoint ISDA as our agent for the limited purposes of the MoU and accordingly we waive, and hereby release ISDA from, any rights, claims, actions or causes of action whatsoever (whether in contract, tort or otherwise) arising out of or in any way relating to this Adherence Email or our adherence to the MoU or any actions contemplated as being required by ISDA.

3. Contact Details

Our contact details for purposes of this Adherence Email are:

Name:

Address:

Telephone:

Fax:

E-mail:

We consent to the disclosure by ISDA of the contents of this letter.

Yours faithfully,

[ADHERING PARTY]

By:

Name:

Title: