



Key data elements to achieve Dodd-Frank compliance

A practical approach

14 June 2011

 **ERNST & YOUNG**
Quality In Everything We Do

Today's agenda

- ▶ About over-the-counter (OTC) derivatives reform
- ▶ How it will impact your business
- ▶ What data elements you will need to capture
- ▶ How the industry is preparing for change

Introduction

The Dodd-Frank Act requires the U.S. Commodity Futures Trading Commission (CFTC) and U.S. Securities and Exchange Commission (SEC) to put in place requirements for reporting swaps and security-based swaps, respectively, to Office of the Financial Research (OFR) data repositories by 15 July 2011.

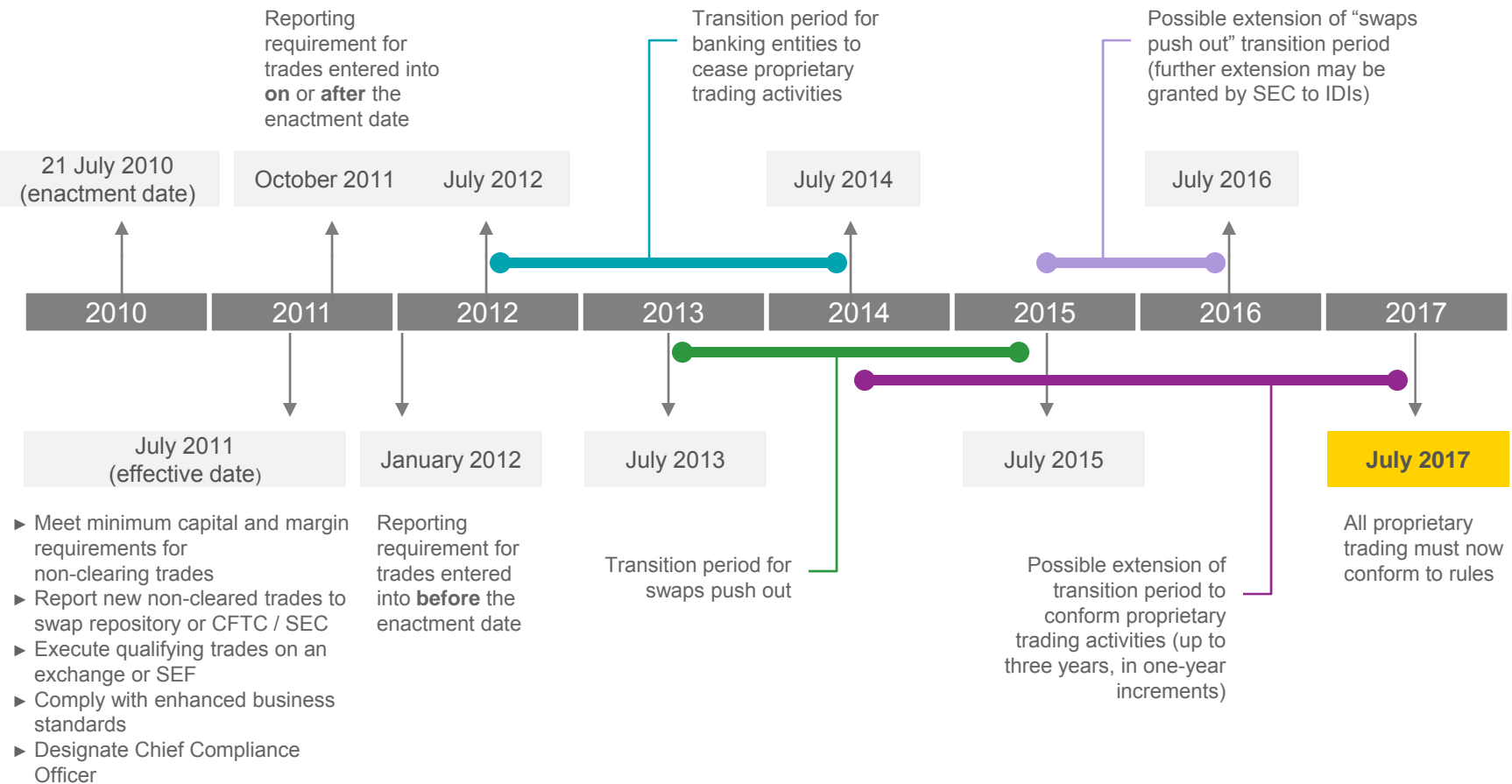
- ▶ Financial institutions are trying to understand reporting and data requirements arising from the Dodd-Frank Act and the potentially broad-based impact on their environments.
- ▶ All of those reporting and data requirements cut across multiple dimensions of the Dodd-Frank Act and apply to a variety of lines of businesses, products, consumers, internal production processes, etc.
- ▶ Ernst & Young has analyzed these reporting requirements to define data classes, subclasses and indicative data elements. We will share a sample of the results of that effort as a baseline for today's discussion.

Summary of OTC derivatives reform

Under Title VII of the Dodd-Frank Act, changes to OTC derivatives will result in:

- ▶ Creation of new designations for market participants
- ▶ Expansion of existing definitions for some existing market participants
- ▶ Supervisory oversight of the OTC derivatives market by CFTC, SEC and prudential regulators
- ▶ Mandated clearing, exchange trading (where available) and reporting for derivatives
 - ▶ Central clearing for standardized derivatives
 - ▶ Exchange trading or execution on Swap Execution Facility (SEF) required if one exists
 - ▶ Reporting of non-standardized trades to swap repositories / CFTC / SEC, including counterparty data
 - ▶ End-user exemption to clearing requirements available, subject to limitations
- ▶ “Push out” of non-standard, non-permitted derivatives to separately capitalized affiliate for Insured Depository Institutions (IDIs) that meet the definition of a swap dealer (SD)
 - ▶ Increased capital requirements for non-standard derivatives
- ▶ Increased margin and capital requirements for financial institutions that meet the definition of a major swap participant (MSP)
- ▶ Enhanced governance and compliance structures for market participants

Current timeline



Assessing the impact by functional area

Business impact	Operations / Process	Technology considerations
Business model: Role, clients, products, services		
<ul style="list-style-type: none"> ▶ SD vs. MSP designation ▶ Designated contract markets (DCM) vs. introducing swap entity ▶ Derivatives clearing organization (DCO) membership financial considerations ▶ Legal entity rationalization and capital and liquidity considerations ▶ Standard contract impact on hedging ▶ Product / client profitability ▶ Competitive positioning 	<ul style="list-style-type: none"> ▶ DCO relationship management ▶ Interfaces with multiple swap entities ▶ Increased risk and capital measurement and reporting ▶ Documentation requirements ▶ Revised compliance processes 	<ul style="list-style-type: none"> ▶ Flexibility of existing infrastructure to connect with multiple DCO / DCM / SR platforms ▶ Increased DCO / exchange volume ▶ Modifications to global on-boarding platforms to reflect regional supervisor requirements
Product mix: Flow and permitted vs. SCA, standardized vs. non-standardized		
<ul style="list-style-type: none"> ▶ Product portfolio composition ▶ Differentiated client service offerings ▶ Pricing considerations ▶ Capital requirements ▶ Product-specific reporting requirements ▶ Financing segmentation 	<ul style="list-style-type: none"> ▶ Process for multiple DCOs with inconsistent rules ▶ Product pricing processes ▶ Product and account/sub-account reconciliations and allocations ▶ Product- and DCO-specific payment and settlement procedures 	<ul style="list-style-type: none"> ▶ Platform reuse flexibility ▶ Product and account reconciliation tool sets ▶ Additional connectivity to DCOs / SRs ▶ Data mining and analytical capabilities

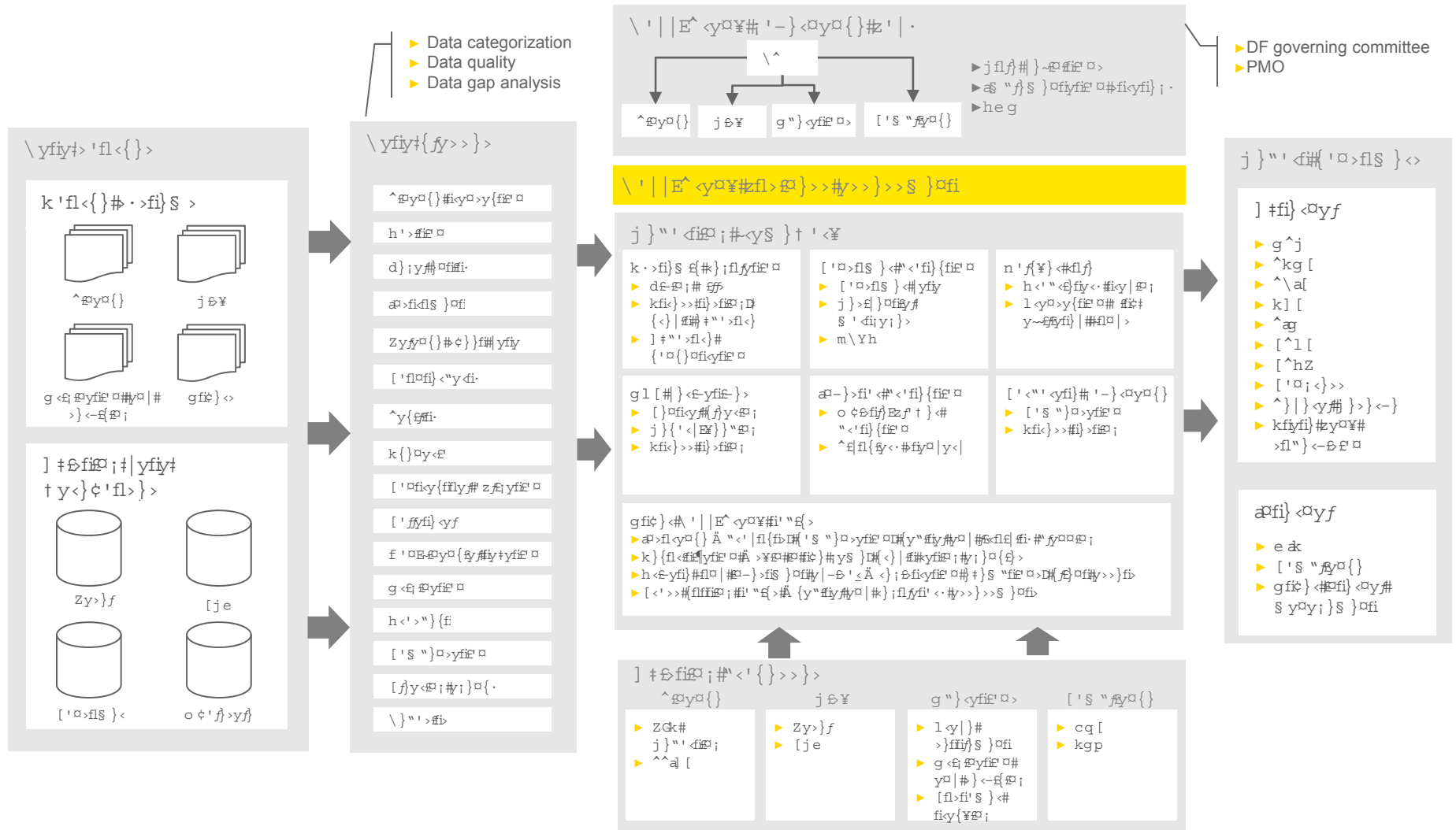
Assessing the impact by functional area

Business impact	Operations / Process	Technology considerations
Client model: Role/Structure, Compliance concerns		
<ul style="list-style-type: none"> ▶ Client service role and interface ▶ Client segmentation and rationalization ▶ Clearing and reconciliation services ▶ Sales credit and compensation structure ▶ Incremental compliance requirements 	<ul style="list-style-type: none"> ▶ Client on-boarding changes ▶ Order management across DCOs ▶ Changes in client account aggregation, disclosures, etc. ▶ End-user considerations ▶ Clearing option process ▶ Fiduciary obligations for “special entities” 	<ul style="list-style-type: none"> ▶ Support new on-boarding procedures ▶ Support variability in initial / variation margin calls ▶ Complexity of client-facing tools ▶ Front office support
Spin off to SCA: IDI / dealer considerations, capital and funding, total vs. partial spin-off		
<ul style="list-style-type: none"> ▶ SCA form / structure / domicile ▶ Identification of capital sources ▶ Governance and risk management ▶ SCA designation (SD or MSP) ▶ Ability of entity to be a DCM 	<ul style="list-style-type: none"> ▶ Ability to leverage existing processes ▶ Intercompany transaction processes ▶ Connections with special-purpose vehicles (SPVs) ▶ Rationalization of product transfers ▶ Enhanced reporting / reconciliation processes 	<ul style="list-style-type: none"> ▶ Information flow and segregation ▶ Service center or separate platform model ▶ Monitor and report risks, capital and activities
Centralized clearing: DCO / DCM, swap repository, exchange / SEF		
<ul style="list-style-type: none"> ▶ Multiple DCO memberships ▶ New DCO / SEF / exchange assessments ▶ Order / customer routing choices ▶ Segregation of cleared and non-cleared product lines 	<ul style="list-style-type: none"> ▶ Multiple confirmation processes ▶ Multiple iterations of “give up” processes ▶ Introducing member firm relationships / platforming ▶ Swap repository reporting for non-standardized trades ▶ “Chinese walls” between DCM entity and remainder of the firm 	<ul style="list-style-type: none"> ▶ Ability to novate trades to and from various swap entities ▶ System capability for cross-DCO data aggregation and reporting ▶ Information security

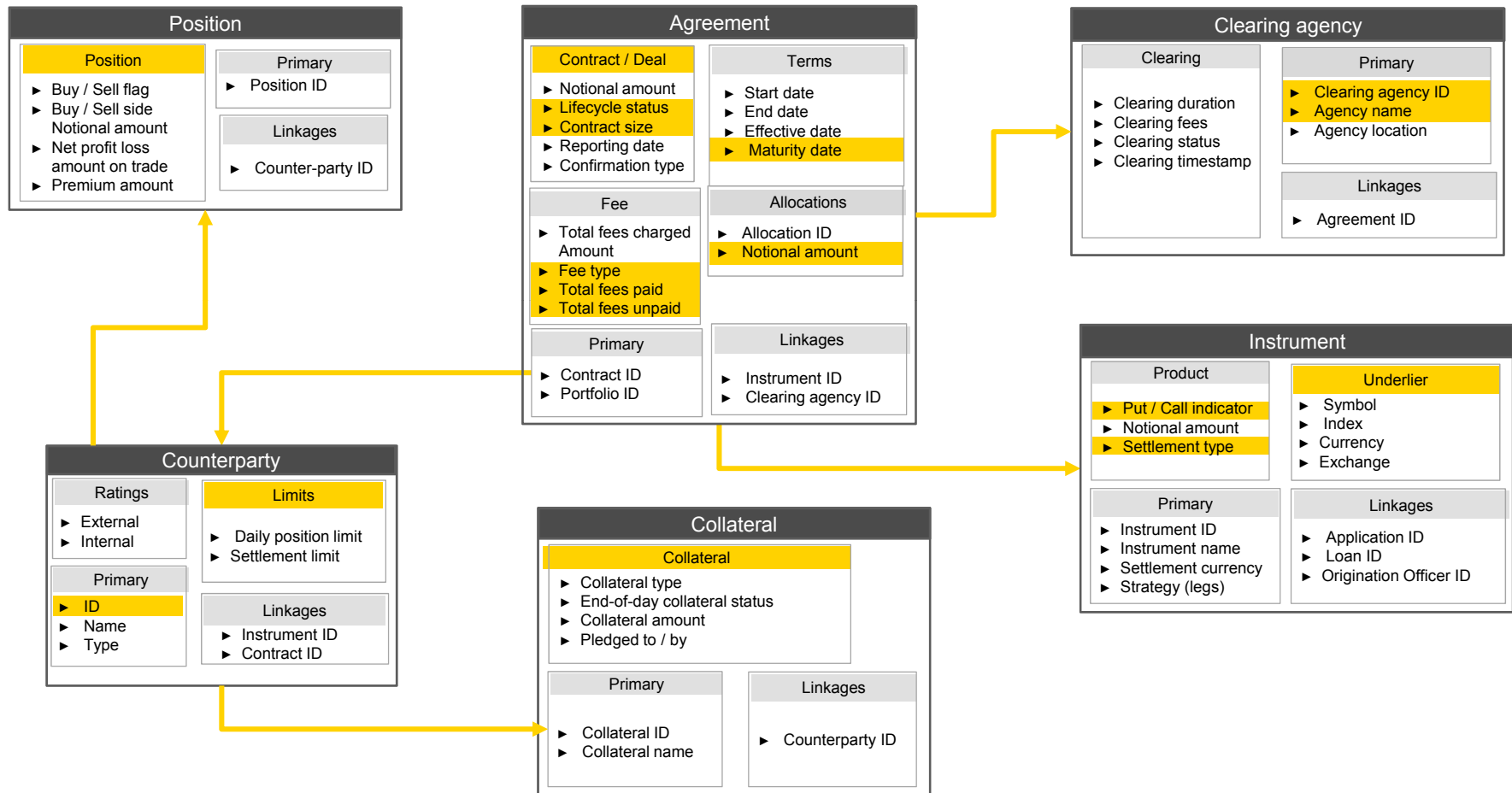
Assessing the impact by functional area

Business impact	Operations / Process	Technology considerations
Collateral management and payments: Margin / Netting, collateral custody, settlement platforms		
<ul style="list-style-type: none"> ▶ Margin monitoring, communication and collection services and costs ▶ Cross-product margining / netting ▶ DCM vs. DCO / third-party custody of collateral / margin ▶ Cash flow / settlement management with swaps entities 	<ul style="list-style-type: none"> ▶ New margin / collateral custody rules ▶ Cross-product netting scope, customer tie-outs and custodial reconciliations ▶ Redefinition of cash flow / settlement process, payment information and related controls ▶ Collateral eligibility, lock-up, replacement and re-hypothecation processes ▶ Customer collateral management and monitoring across DCOs ▶ Client payment management and tracking across sub-accounts 	<ul style="list-style-type: none"> ▶ Ability to leverage existing collateral management and netting, payment and settlement platforms for: <ul style="list-style-type: none"> ▶ Reconciliations with custodians / client accounts, DCOs ▶ Connections through industry payment utilities ▶ Predictive modeling ▶ Further parameterization of international swaps and derivatives association credit support annex
Reporting: Regulatory bodies, DCO / repositories, customer management		
<ul style="list-style-type: none"> ▶ Enhanced management / P&L reporting and other management information ▶ Client confidentiality concerns ▶ DCO vs. swap repository for reporting of cleared and non-cleared transactions 	<ul style="list-style-type: none"> ▶ Revised reporting processes and controls ▶ Enhanced information gathering and aggregation with respect to pricing, volumes, terms and conditions, margin, capital requirements, etc. ▶ Controls around completeness and accuracy of data and segregation of information 	<ul style="list-style-type: none"> ▶ Metadata models ▶ Additional data feeds and extract, transform, load (ETL) to enable data sourcing for new reporting ▶ Extensible tool sets to aggregate virtual and physical pools and data quality

Dodd-Frank data class and reporting framework



Snapshot of the OTC derivatives data model



Legend: **Yellow** highlight indicate a new or modified data class / data attribute / data linkages

High-level data impacts

Reporting requirements	Description	Data impacts
Counterparty report with position limits	<ul style="list-style-type: none"> ▶ Counterparty details and position limits need to be reported by: <ol style="list-style-type: none"> 1. Derivatives clearing organization 2. Board Of Trade (Exchanges) 3. Swap execution facilities 	Counterparty ▶ Counterparty ID, counterparty daily settlement limit, customer limit, materiality flag, date of incorporation, intercompany indicator
		Position ▶ Position ID, counterparty daily position limit, start date, maturity date, replacement cost, profit or loss amount
		Clearing agency ▶ Clearing agency ID, clearing agency name, clearing duration, clearing status, clearing fees
Settled and cleared derivative <ul style="list-style-type: none"> ▶ Contract term and conditions details ▶ Clearing fees and other fees charged 	<ul style="list-style-type: none"> ▶ Most derivatives will be required to clear through central clearing agencies to reduce highly interconnected and often unfunded counterparty risk exposures. ▶ To comply, a financial institution needs to report the terms and conditions of each contract, agreement and transaction cleared and settled by the derivatives clearing organization. 	Contract / agreement ▶ Contract ID, contract type, contract effective date, maturity date, lifecycle status code, contract quantity, date of clearance, buy / sell side notional amount
		Instrument ▶ Instrument ID, instrument type, instrument name, settlement type, index (commodity, security, loan, etc.), Symbol, put / call indicator
		Fees ▶ Total fees charged amount, total fees paid amount, total fees unpaid amount, commission

High-level data impacts

Reporting requirements	Description	Data impacts
Collateral end-of-day under margin report	<ul style="list-style-type: none"> ▶ End-of-day collateral status against each must be reported and split by liquid collateral type. This is to ensure that SDs and MSPs are subject to capital and margin requirements. 	Counterparty ▶ Counterparty ID, counterparty name, master netting agreement identifier, business segment, SME flag
		Collateral ▶ Collateral type, collateral rating date, collateral amount, pledge in / out code, premium paid, premium unpaid, premium charged
Swap trade report and position limits	<ul style="list-style-type: none"> ▶ Daily reports of all trades and positions with counterparty limits for swaps. For record-keeping, this data needs to be maintained for five years. 	Contract / agreement ▶ Contract ID, contract type, settlement type, effective date, maturity date, life cycle status code, contract quantity
		Position ▶ Position ID, counterparty daily position limit, realized / unrealized profit / loss amount, buy / sell side replacement cost amount, net profit loss amount on trade
Segregated collateral reporting	<ul style="list-style-type: none"> ▶ Collateral data needs to be reported for all cleared and uncleared deals. The report should provide required information to prove that the broker, dealer or security-based swap dealer is keeping the customer collateral. 	Collateral ▶ Collateral type, collateral amount, collateral appraisal amount, collateral rating code, collateral unit count, lien status, currency code, pledge party ID
		Counterparty ▶ Pledge party ID, pledge party name, pledge to / by counterparty, bank / non-bank flag, creation date, location code, external / internal credit score

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