

# **TASK FORCE ON CONFIRMATIONS**

## **PROGRESS REPORT**

# AGENDA

- Initial key questions
  - Scope in terms of products
  - Scope in terms of counterparties
  - Roles and objectives of the taskforce
- Recommendations (examples)
- Discussion topics
  - Phone confirmations
  - On line trading

# AGENDA

- Discussion topics (continued)
  - How to improve exchange of confirmations with non banks ?
  - How to improve the STP level in confirmations processing ?
  - Move of confirmations to front office : impact of some market evolutions

# **INITIAL KEY QUESTIONS**

# SCOPE IN TERMS OF PRODUCTS

- Most existing recommendations focus on forex and money market (ACI, London FX Committee, ...)
- This is also the scope of the two parent groups of the OMG
- Nevertheless the taskforce proposes to cover the entire scope of transaction types

# SCOPE IN TERMS OF PRODUCTS

- Forex – Money Market :
  - Spot, Forward, Swap
  - NDF
  - Loans/deposits
  - Call notice
- OTC Derivatives
  - Fx derivatives
  - IR derivatives

# SCOPE IN TERMS OF PRODUCTS

- Equity derivatives
- Credit derivatives
- Commodity derivatives (including energy)

Need to differentiate between “plain vanilla”, exotic and structured

- Securities
  - Buy and sell trades
- Repo & securities lending

# SCOPE IN TERMS OF PRODUCTS

- Depending on the product the issues are different
- Forex and money market : non banks
- Derivatives : STP level, need for standards
- Securities : confirmations are probably “less” important as focus is on pre-settlement matching and DVP settlement



# SCOPE IN TERMS OF COUNTERPARTIES

- Financial transactions are dealt with a wide range of counterparties
- The taskforce proposes the following classification :
  - Banks
  - Non banks with
    - Large corporates
    - Small corporates
    - Funds and hedge funds
    - Other smaller clients (retail)

## **ROLES AND OBJECTIVES OF THE TASKFORCE**

- Initial purpose was to issue a set of recommendations or best practices regarding confirmations
- The taskforce believes this kind of recommendations will add little value to already existing recommendations
- On top of issuing some fundamental recommendations the taskforce proposes some other initiatives :

# **ROLES AND OBJECTIVES OF THE TASKFORCE**

- Lobbying on a number of associations, institutions
- Discussing at the OMG some topics relevant to the market industry, try to identify some best practices and encourage their adoption by market participants

# **RECOMMENDATIONS**

# RECOMMENDATIONS

- On next pages : some examples of recommendations (draft)
- Some references :
  - The confirmation or automatic matching of transactions (ACI Model Code)
  - Confirmation Processing – a good practice guide (London FX Committee)
  - Some extracts of the “Corigan report” – Counterparty Risk Management Policy Group

# RECOMMENDATIONS

- Exchange of bilateral confirmations should be the rule
- Confirmations should be issued as soon as possible after trade execution
- Banks should favour the use of electronic formats (“standard messages”) in order to increase speed, allow full tracability and implementation of automatic matching

# RECOMMENDATIONS

- Encourage participation in market initiatives like matching utilities (DTCC for credit derivatives, Swapswire for interest rate derivatives, ...)
- Banks should consider confirmations matching as a key risk mitigating factor and allocate enough resources to that function (skilled staff and adequate systems)

# RECOMMENDATIONS

- Management reporting should be available and closely monitored (number of outstanding items, aging, ...)



# **DISCUSSION TOPICS**

# PHONE CONFIRMATIONS

- Phone confirmations should be avoided
- Confirmations should be as much as possible be issued :
  - In electronic structured format
  - Using standard messages
  - Through a secure way of communication
- Phone confirmations should only be used as a fall back solution (chasing)

# ON LINE TRADING

- Automated trading systems have taken a major place in the marketplace
- Some examples :
  - EBS and Reuters Matching in the fx professional market
  - Multibank portals like FXALL in the corporate market
  - MTS and Brokertec in the bonds and repo market
  - Internal web based tools
- Regularly the question of the need to maintain the exchange of confirmations for this type of trades is raised

# ON LINE TRADING

- The Taskforce is of the opinion that continuing to send confirmations reduces the overall level of operational risk
- Even if the presence of a trade in a deal blotter might be binding, the issuance of a confirmation has an added value :
  - Protection against fraud, hacker, ..
  - We do not know the STP level of our couterparties
  - Confirmations are often more complete

# ON LINE TRADING

- Nevertheless the Task Force believes there will be forces to go away from confirmations exchange in some cases and banks will need some flexibility :
  - Need for confirmations for securities trades where there is DVP settlement (and sometimes “delegation” of settlement initiation to market like MTS) ?
  - Need for chasing “on line trades” which are already settled ?
- But going away from the bilateral exchange should always be agreed bilaterally

# HOW TO IMPROVE EXCHANGE OF CONFIRMATIONS WITH NON BANKS

- The issue seems to be “cultural”. This best practice does not seem to be perceived as important by clients.
- Involve sales people in the “education” of the client
- Involve corporate audit firms ?
  - They could insist on the importance of checking confirmations and returning them to banks
  - This topic could be part of their audit reviews
  - Can the OMG play a role in this respect ?

# HOW TO IMPROVE EXCHANGE OF CONFIRMATIONS WITH NON BANKS

- Should banks encourage clients to move to solutions like Misys or CLS ?
- Should regulators intervene and require provisions or “charge” capital for outstanding confirmations ? (in order to force banks to take actions)

# HOW TO INCREASE STP IN CONFIRMATIONS PROCESSING ?

- Although standards exist for some products (MT305, 306), Swift is still “underused” by banks. Idem for NDF’s. Extension of usage should be encouraged.
- Initiatives like Swapswire or DTCC have clearly improved the STP level and contributed to the reduction of backlogs. So participation should be encouraged, but access for “smaller” counterparts remain difficult.



# HOW TO INCREASE STP IN CONFIRMATIONS PROCESSING ?

- Lobbying on Swift (or others like Misys) to extend coverage ?  
ex : fixing on NDF, ...
- Avoid ISDA long form confirmations ? i.e. Negotiate Master Agreement first and do not repeat ISDA Definitions or Master Agreements clauses in trade confirmations

# CONFIRMATIONS CLOSER TO FRONT OFFICE ?

- Initiatives like Swapswire have moved the confirmations task from back to front office
- Similarly the process of “affirming” trades have moved us away from the bilateral exchange of confirmations
- These evolutions are in contradiction with some existing “best practices” or recommendations. Issue ?

# CONFIRMATIONS CLOSER TO FRONT OFFICE ?

- The Task Force considers these initiative as positive. However banks should give attention to the overall level of operational risk. Some attention points :
  - STP level from FO systems to BO systems
  - Coherence of the data between both systems (need for reconciliation)
  - Potential need for periodic reconciliation with external data