

Commodity Futures Trading Commission

via Website Submission

Re: RIN 3038–AC97, Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants – TriOptima comments

Dear Sir/Madam,

Background

TriOptima is a provider of post-trade risk reduction services and operates triReduce, a compression service run in cycles where two or more market participants submit existing OTC swap portfolios in order to reduce counterparty credit risk, the number of outstanding swaps and/or the outstanding notional amount under their respective swap portfolios. To date, triReduce has facilitated the compression of more than 510 trillion USD in notional amounts in interest rate, credit default and commodity swaps. The triReduce portfolio compression exercises cover both cleared and uncleared OTC swaps. TriOptima also offers triBalance, a counterparty risk rebalancing service for OTC swap portfolios.

TriOptima welcomes the CFTC seeking public comments on the proposed rule setting out proposed margin requirements for uncleared swaps for Swap Dealers and Major Swap Participants (the "Proposed Rule"). As a leading provider of post-trade risk reduction services we acknowledge that the content of the Proposed Rule is of significant interest both to us and our clients.

References and defined terms used in this document but not defined herein refer to the corresponding references and defined terms in the Proposed Rule.

One key element in the development of markets and post-trade legislation has been the treatment of post-trade risk reduction services. These services are generally encouraged by legislators as they reduce outstanding risk in the financial markets, thus reducing the likelihood of another financial crisis. The CFTC has previously noted that portfolio compression is an "*important post-trade processing mechanism[s] for reducing risk and improving operational efficiency*", and we note

TriOptima AB
PO Box 182
101 23 Stockholm
Sweden

Tel +46 8 545 25 130
Fax +46 8 545 25 140
Company reg no. 556584-9758

Courier address: Blekholmsgatan 2F
111 64 Stockholm
Visiting address: Klarabergsviadukten 63



that the CFTC explicitly points to one such risk reducing effect on p. 59924 of the Proposed Rule, mentioning how concerns around concentration of risk may be mitigated “*by performing frequent portfolio compression exercises*”.

Post-trade risk reduction services in legislation

CFTC rulemaking under the Dodd-Frank Act recognizes the value of post-trade risk reduction services and explicitly requires Swap Dealers and Major Swap Participants to “*establish, maintain, and follow written policies and procedures for [...] periodically engaging in multilateral portfolio compression exercises [...]*” in relation to uncleared swaps.

The CFTC has also previously granted explicit no action relief for “*any person for failure to comply with the requirement under section 2(h)(1)(A) of the CEA and part 50 of Commission regulations to clear an amended swap or a replacement swap that is generated as part of a multilateral portfolio compression exercise*”.

In the EU, the MiFIR regulation has expanded on the definition of post-trade risk reduction services, not merely limiting it to post-trade compression services, by highlighting that “*the obligation to conclude transactions in swaps pertaining to a class of swaps that has been declared subject to the trading obligation on a regulated market, MTF, OTF or third country trading venue should not apply to the components of non-price forming post-trade risk reduction services which reduce non-market risks in swaps portfolios including existing OTC swaps portfolios in accordance with Regulation (EU) No 648/2012 without changing the market risk of the portfolios. In addition, while it is appropriate to make specific provision for portfolio compression, this Regulation is not intended to prevent the use of other post-trade risk reduction services.*” (MiFIR, Recital 27).

Scope of activities

The examples further underline the importance of post-trade risk reduction services in financial markets both today and in the future.

The scope of activities that would classify as post-trade risk reduction services is limited as these services only aim at reducing risks for swaps transactions already entered into. Examples of specific post-trade risk reduction services include:

- **Portfolio compression:** Counterparties wholly terminate or change the notional value of some or all of the swaps submitted by the counterparties and depending on the methodology employed, replace the terminated swaps with other swaps whose combined notional value is equal to or less than the combined notional value of the terminated swaps in the compression exercise.
- **Counterparty risk rebalancing:** Counterparty risk management that rebalances counterparty risk exposure between multiple CCPs and bilateral relationships.

Post-trade risk reduction services are typically cycle-based and multilateral, and as indicated above “new” swap transactions may be created as part of the “compound transactions” resulting from these cycles – albeit that these swap transactions are not trading transactions but serve the purpose of either replacing partially terminated swap transactions or rebalancing counterparty risk exposure.

A compound transaction may contain thousands of component swap transactions, but it is worth noting that in terms of counterparty risk rebalancing services, the vast majority of such component swap transactions will be clearable plain vanilla swap transactions subject to the clearing mandate, with only a limited number of structured unclearable swaps (which offset risk in the legacy uncleared portfolio).

Bilateral margining and post-trade risk reduction services

The scope of the bilateral margining proposal as presented in the Proposed Rule does not specifically address or accommodate post-trade risk reduction services. In fact, in the absence of any clarifying provision, and to the extent that any resultant swap transaction would require initial and variation margin payments, legacy portfolios (consisting of trades entered into before the applicable compliance dates as set out in §23.159 of the Proposed Rule) would be significantly dis-incentivized from the use of post-trade risk reduction services, as such post-trade risk reduction component swap transactions would be subject to margining requirements that did not apply when the original transactions were entered into. Further, for counterparty risk rebalancing services adjustments must be made to the cash flows belonging to the same netting set from which the bilateral risk emerges, in order to achieve the intended reduction of bilateral portfolio risk. Accordingly, to the extent the Proposed Rule has the effect that transactions resulting from post-trade risk reduction services are not allowed be maintained in the same netting set as that from which the bilateral risk emerges, the Proposed Rule may risk significantly decreasing the efficiency of, and dis-incentivizing market participants from using, such services.

In order to align the treatment of post-trade risk reduction services in the Proposed Rule with existing Dodd-Frank Act provisions and CFTC rulemaking, as set out above, we would urge the CFTC to consider classifying transactions that result from post-trade risk reduction services on legacy portfolios equally as legacy transactions that (i) do not require the posting of collateral for the purposes of the Proposed Rule, and (ii) are allowed to be maintained in the same netting sets from where the risk emerged.

To assist the drafting, we have suggested below some key components that define these post-trade risk reduction services and that could serve as a basis for classifying these services in legislation:

“Components of non-price forming post-trade risk reduction services which reduce non-market risks in swaps portfolios shall mean only components of a compound transaction where:

- *the transaction is designed to be overall market risk neutral for each participant;*
- *the participants of the transaction do not submit bids and offers to enter into a specific position;*
- *the transaction is cycle-based and multilateral (e.g. including at least two participants), and must be accepted in full by all participants or it will not be effected; and*
- *the transaction is designed to reduce secondary risks emerging from existing swaps transactions, such as counterparty credit risk, operational risk and/or basis risk.”*

Conclusion

We would urge the CFTC to consider classifying transactions that result from post-trade risk reduction services on legacy portfolios equally as legacy transactions not subject to the obligations under the Proposed Rule.

Please note that TriOptima requests that this letter should be treated confidentially and thus withheld from publication by the CFTC.

We are happy to provide further information on the above, if and as required.

Sincerely,

Per Sjöberg
Group Chief Executive Officer
TriOptima

Christoffer Mohammar
General Counsel
TriOptima

