INSTITUTIONALLY MANAGING YOUR TRADING RELATIONSHIPS

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Is it really that important to spend time and money negotiating the terms of my trading and financing agreements? Why? It's really all about relationships, isn't it? Are some terms more important than others?

On a day-to-day basis, clients aren't looking through their trading agreements. If they have a question, they call their contact at the dealer who susses out the answers by calling his or her legal or ops team. This may not be an option in times of uncertainty but such times are when a firm's knowledge of the terms of its relationship is critical. The uncertainty can be market-related or could be due to something that happens within a firm.

For example, when Lehman filed for bankruptcy, firms needed to quickly understand the terms of their agreements, from the most basic information to a more nuanced understanding of their collateral rights. Their contacts at Lehman weren't there to answer their questions – in fact, no one was answering their phones at all. First, there was a scramble to find agreements and then, to locate attorneys that could review hundreds of pages to answer questions such as: *What entities am I facing under these contracts? Where are my assets held? Can I get my collateral back? What is my exposure to these entities? Can the bankrupt entity grab the collateral held under the other agreements with other Lehman entities?*

Other less-world-changing events can also impact your relationships. For example, If LIBOR – OIS spreads widen out, can a dealer change your financing rates or terminate your relationship? At a firm level, inflection points, such as the departure of a key person or an SEC investigation, can trigger termination rights and notification obligations.

If you have one or two PB relationships, a few ISDAs and a couple of futures accounts, you can have your attorney provide you with a detailed summary of your more important provisions. It's a little expensive, but your information will be there when you need it. You just have to remember to update and maintain these summaries as your relationships with dealers evolve.

If you have multiple entities with many trading relationships, the spreadsheet option is no longer a viable solution. A fund manager with four trading entities, each of which have three or four PB agreements, ten or more ISDAs, three or four futures agreements, and several repurchase agreements, options agreements, total return swaps and execution agreements will have hundreds or thousands of documents across possibly dozens of dealer relationships to track. Additionally, based on the strategies and jurisdictions of each trading entity, the agreements with a dealer can differ from entity to entity. Manual summaries are unreliable and the upkeep of this information without structure becomes unmanageable.

I receive a phone call several times a year where a client describes some event and ask us to look into its impact on their agreements. Our team drops what we are doing and pull all of the agreements that we and the client can locate. We then pore over each agreement to determine the applicable provisions and impact of the event to provide the client with an update. This process sometimes takes days or weeks and I worry about missing something. This type of review is expensive and time consuming.

The events of 2007 and 2008 also evidence the importance of promptly accessing and negotiating the terms of these agreements. Market events and firm events occurring at once require a good grasp of agreement triggers, which is critical to maintaining and strategically managing a firm's stability. In my prior life at a hedge fund, during such times, knowing and consciously negotiating the terms of our agreements enabled us to push back on actions that could have hurt the business. Our terms gave us bargaining power that we otherwise would not have had.

Seeing this need for information quickly and how opaque these agreements can be (similar in substance, but often varying in form from dealer to dealer), our firm has developed a web based application to store, track and organize the material terms of trading and financing agreements. Our tool, Koya DocuTracker, was developed with a focus on industry terms and is not specific to any one dealer. The functionality stores and organizes over 25 trading and financing agreements. It also tracks and provides reporting on hundreds of material economic, credit and legal terms in these agreements and across dealers. The answers are summarized into plain English answers and available at the click of a button.

To be institutional and truly manage the stability of a trading firm's business, it is crucial in the most extreme times to know and quickly access the terms of the agreements that form the foundation of your business. Whichever way you choose to do this, it should be reliable, readily available, and comprehensive.

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