

BY EMAIL

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Ladies and Gentlemen

ISDA comments on the FCA's Consultation Paper CP14/15 on the transposition of the Recovery and Resolution Directive, published 1 August 2014

The International Swaps and Derivatives Association, Inc. (**ISDA**)¹ is grateful for the opportunity to provide input to the Financial Conduct Authority's (**FCA's**) Consultation Paper (CP14/15) on the transposition of the Recovery and Resolution Directive, published 1 August 2014 (the **Consultation**).

Consistent with our mission, we are primarily concerned in this letter with the impact of the proposed implementation on the safety and efficiency of the financial markets, by considering the direct impact of the proposals on the obligations of firms with respect to derivatives and other financial transactions, and the consequential impact on market counterparties to such financial transactions in the event that a firm goes in to resolution. We are aware that a number of other market associations and professional bodies will be responding on some of the broader issues raised by the Consultation.

ISDA supports the FCA's proposals for changes to its Handbook in order to transpose the Recovery and Resolution Directive (**BRRD**), although ISDA defers to those of its member firms who will be directly affected by the proposals and is itself concerned only with limited aspects of the proposals. Given ISDA's remit we limit our response to Chapter 6 of the Consultation (contractual recognition of bail-in). Question 15 of the Consultation reads as follows:

¹ Information regarding ISDA is set out in Annex 1 to this response.

Q15: Do you agree with our transposition of the Directive provisions relating to contractual recognition of bail-in and do you have a view regarding the date of the commencement of this provision?

Yes, ISDA supports the FCA's approach to implementation of Article 55 of the BRRD. In particular, ISDA supports the FCA's position as regards the date of implementation.

The interpretation of Article 55 of the BRRD poses a number of difficult questions for affected firms. In particular, for parties to derivatives contracts, which are ordinarily documented under industry standard master netting agreements (such as the ISDA Master Agreement) and which, under Article 49 of the BRRD, can only be subject to bail-in after they have been closed out, the point in time at which the relevant liability is issued or entered into is not straightforward. To illustrate, a master agreement may have one derivative contract entered into on 1 January 2012, and a second on 1 February 2015; in the event that the derivatives are to be bailed-in, derivatives contracts one and two must each be closed-out and a single net sum determined. This first derivative contract is, *prima facie*, outside of the scope of Article 55. However, given that only the net sum is subject to bail-in, it would seem odd for recognition to be required on a contract by contract, and not on a master agreement, basis. These questions, and others, are being considered by the European Banking Authority (the **EBA**) in detail as they develop the regulatory technical standard (RTS) required by Article 55(3) of the BRRD.

Without any further guidance, whether in the form of the EBA RTS or (in advance of such RTS) PRA guidance, there is a risk that different firms will take considerably different approaches to the interpretation of Article 55.

Accordingly, ISDA considers that delaying implementation of Article 55 until such time as the EBA's guidance is available is entirely sensible.

We hope that you find our comments useful in your continuing deliberations on the transposition of the BRRD. Please do not hesitate to contact either of the undersigned if we can provide further information about the derivatives market or other information that would assist the FCA in its work in relation to the Handbook or, more broadly, the effective transposition of the BRRD.

Yours faithfully

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ABOUT ISDA

Since its founding in 1985, the International Swaps and Derivatives Association has worked to make over-the-counter (OTC) derivatives markets safe and efficient.

ISDA's pioneering work in developing the ISDA Master Agreement and a wide range of related documentation materials, and in ensuring the enforceability of their netting and collateral provisions, has helped to significantly reduce credit and legal risk. The Association has been a leader in promoting sound risk management practices and processes, and engages constructively with policymakers and legislators around the world to advance the understanding and treatment of derivatives as a risk management tool.

Today, the Association has more than 850 members from 63 countries on six continents. These members include a broad range of OTC derivatives market participants: global, international and regional banks, asset managers, energy and commodities firms, government and supranational entities, insurers and diversified financial institutions, corporations, law firms, exchanges, clearinghouses and other service providers.

ISDA's work in three key areas – reducing counterparty credit risk, increasing transparency, and improving the industry's operational infrastructure – show the strong commitment of the Association toward its primary goals; to build robust, stable financial markets and a strong financial regulatory framework.

The addresses of our European offices are as follows:

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Our registration number in the relevant EU register is 46643241096-93.

More information about ISDA is available from our website at <http://www.isda.org>, including a list of our members, the address of our head office in New York and other offices throughout the world and details of our various Committees and activities, in particular, our work in relation to financial law and regulatory reform.