ISDA Welcomes European Commission’s Recognition of the Vital Role Played by OTC Derivatives; Urges Caution on Mandated Clearing or Exchange Trading

NEW YORK, Tuesday, October 20, 2009 — The International Swaps and Derivatives Association welcomes the European Commission’s continued recognition of the important role derivatives play in the economy, as expressed in the EC’s Communication outlining future policy actions on derivatives markets. ISDA looks forward to continuing to work with the Commission as it finalizes its policies.

“ISDA and the industry have achieved significant progress improving and standardizing various derivatives markets, including CDS, and we look forward to continued success in collaboration with the Commission,” commented Robert Pickel, Executive Director and Chief Executive Officer, ISDA. “At the same, we want to make sure that any new policies or regulations preserve and enhance the critical ability of market participants to manage their risk exposures.”

ISDA believes proper consideration should be especially given to any policy requiring that standardized OTC trades be conducted on an exchange or electronic trading platform. In light of the G20’s recent agreement that exchange trading should take place “where appropriate,” ISDA thinks the benefits, as well as the drawbacks, of exchange trading now need to be carefully weighed.

Mandated exchange trading could limit the flexibility of derivatives users to hedge their risk exposure. Some forms of price disclosure and inappropriate forms of standardization will harm liquidity by disincentivizing participation in derivative markets.
ISDA strongly supports the Commission’s call for greater transparency. Indeed, the Association has worked hard to increase transparency, including working with buy-side and dealer firms on such initiatives as the Credit Derivatives Determinations Committee. Additionally, ISDA is helping to significantly increase the flow of information to regulators, as well as to the general public. For example, the Association has made available to all market participants a CDS standard model that improves consistency and reduces operational differences regarding the calculation of CDS prices.

ISDA has also recently announced the formation of an FpML Working Group whose focus is on the reporting of OTC derivatives positions and regulatory reporting. ISDA is working hard to ensure regulators have complete access to trade information through trade repositories and the Working Group is focusing on extending current FpML standards to standardize reporting communications with the repositories. At the same time, however, the Association cautions against indiscriminate release of trade prices, which may undermine liquidity.

ISDA is also committed to the increased use of central clearinghouses. ISDA and 15 large derivatives dealers have publicly committed to international regulators that the firms would submit 95% of new eligible credit default swap trades for clearing by October of 2009 and 90% of new eligible interest rate swap trades beginning in December 2009. CCPs for the credit default swap and interest rate markets are fully operational in Europe and the USA and are being used by major dealers. At the same time, however, the Association is concerned that mandating central clearing or too strongly incentivizing the use of a central clearing partner would increase costs disproportionately and severely constrict the ability of market participants to appropriately manage their risk.

ISDA is pleased that the European Commission recognizes the vital role OTC derivatives play in hedging risk that arises in business and that it does not want to limit the economic terms of derivative contracts, prohibit their use or make them excessively costly. Companies ranging from auto makers to airlines rely on derivatives to manage an array of risks, including interest rate and currency changes. ISDA strongly believes increasing collateral requirements on non-financial institutions could be excessively burdensome. ISDA looks forward to working with regulators on the recently publicized international regulatory initiative focusing on an appropriate collateralization framework for bilateral transactions, further enhancing the risk management tools ISDA and the industry have developed over the past two decades.

About ISDA
ISDA, which represents participants in the privately negotiated derivatives industry, is among the world’s largest global financial trade associations as measured by number of member firms. ISDA was chartered in 1985, and today has over 830 member institutions from 58 countries on six continents. These members include most of the world’s major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the financial market risks inherent in their core economic activities. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

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