REGULATION
ESMA's Verena Ross on regulatory simplification

MARGIN
Reflections on a decade of the ISDA SIMM

CAPITAL
EBA's Lars Overby on the need for a level playing field

IQ
ISDA® Quarterly

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* CALIBRATION TEST

With Basel III nearing completion, the success of the capital framework depends on risk-sensitive adjustments and consistent implementation

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ISDA® Safe, Efficient Markets

A Decade of the ISDA SIMM

Ten years ago, the derivatives industry began implementing one of the most far-reaching regulatory reforms ever introduced: the margin rules for non-cleared derivatives. This posed a unique challenge. Both counterparties would need to agree on the amount of initial margin to exchange, but if every firm used its own proprietary model, the numbers probably wouldn't match. The result? Endless disputes and operational headaches that could have caused trading to grind to a halt.

This led to something that had never been done before – the coming together of the industry under the ISDA umbrella to build a transparent and standardized model that everyone could use. A decade on, the ISDA Standard Initial Margin Model (ISDA SIMM) is permitted for use by regulators in more than 40 countries, is used by over 440 groups of entities and is supported by 70 vendors. Throughout that time, the ISDA SIMM has been continually refined and tweaked to ensure it remains risk-appropriate, overseen by a global community of regulators. Importantly, the success of the ISDA SIMM also set a precedent for the industry to come together through ISDA to tackle other big market structure challenges, including the transition from LIBOR.

In this issue of **IQ**, we look back at the factors and decisions that shaped the development of the ISDA SIMM and consider how the model may evolve in the years ahead.

The ISDA SIMM was based on a model proposed by regulators as part of the Fundamental Review of the Trading Book. Earlier this year, implementation of those market risk capital standards took a big step forward in the US with a revised set of proposals from prudential regulators. While the Basel III endgame proposal is much more risk-sensitive than earlier versions, more work is needed to ensure capital requirements are fully aligned with risk. That includes refining the methodology so offsets within portfolios of derivatives and repos are appropriately recognized when calculating capital under the standardized approach for counterparty credit risk. Our cover story examines the progress that has been made and the key challenges that still need to be resolved.

Nick Sawyer
Global Head of Communications & Strategy
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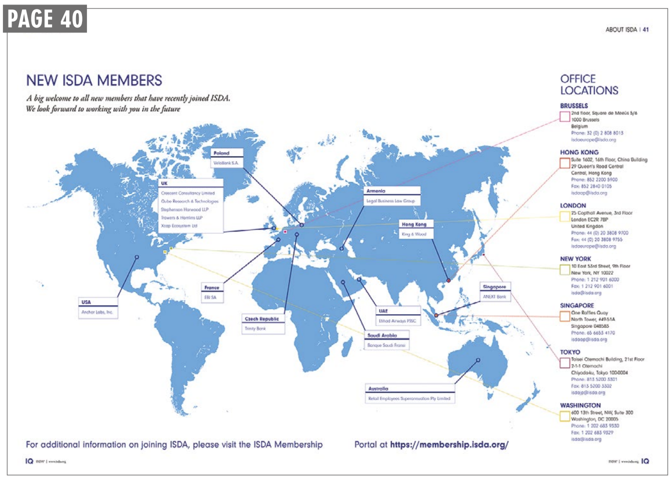

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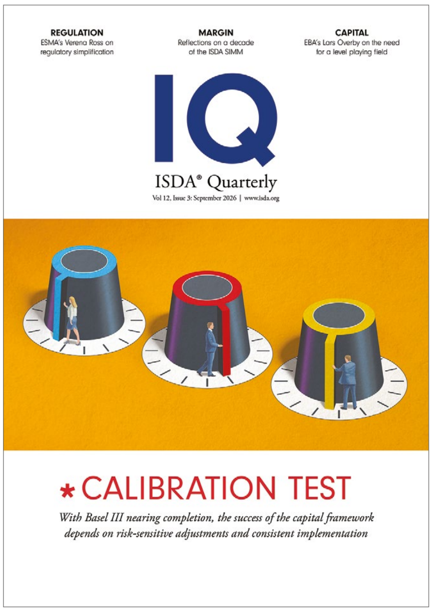

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"A level playing field is clearly needed, both to ensure that banks can compete on equal terms, but also to ensure the prudential framework reflects the risks in a comparable manner, so investors can meaningfully assess the risks of banks"

Lars Overby, European Banking Authority

Pursuing Efficiencies

As the ISDA SIMM marks its 10-year anniversary, a continued focus on efficiency can help unlock the potential of tokenization and 24/7 trading, writes ***Scott O'Malia***

This month marks 10 years since the launch of the ISDA Standard Initial Margin Model (ISDA SIMM), which coincided with the first phase of initial margin (IM) requirements for non-cleared derivatives in September 2016. The ISDA SIMM was a pioneering industry solution that addressed a shared problem arising from the new rules – if every firm developed its own model to calculate IM, there would have been chaos, with disputes, delays and increased risk. The advent of a transparent, industry-standard model enabled successive waves of firms subject to the margin rules to agree IM amounts quickly and efficiently.

Ten years on, the ISDA SIMM is a cornerstone of the non-cleared derivatives market infrastructure. The model is permitted for use by regulators in more than 40 countries, used by more than 440 groups of entities and supported by 70 vendors. ISDA has never stopped evolving the ISDA SIMM, with 17 updates so far to ensure it remains risk-appropriate, reflecting changing market conditions, new products and evolving risk dynamics. On top of that, ISDA shares detailed calibration, backtesting and performance-monitoring information with global regulators and maintains regular dialogue on the model's evolution.

The success of the ISDA SIMM has been driven by a relentless focus on maintaining its risk sensitivity, in collaboration with global regulators, which has enabled the efficient exchange of margin at scale. Of course, ISDA's drive towards greater efficiency extends well beyond the calculation of IM. Through our set of mutualized solutions, we've brought significant improvements to vital industry processes, from the negotiation of documentation and the delivery of termination notices to the implementation of reporting rules. We're now heavily focused on two areas where we believe significant operational efficiencies and economic value can be delivered by the adoption of new technologies at scale – tokenization and 24/7 trading.

By enabling near-instantaneous settlement, tokenized assets could reduce counterparty risk, enable intraday liquidity management and increase the mobility of collateral. Tokenization could also open the door to money market funds being posted as collateral, eliminating the barriers that had previously prevented market participants from reducing their reliance on cash and government securities.

"ISDA is well advanced in building the standards, documentation and infrastructure to advance tokenization responsibly and support the transition to 24/7 trading"

As with any innovation, there are legal, regulatory and operational hurdles to be overcome to realize the potential efficiencies that tokenization offers. Questions relating to custody and segregation frameworks, capital and margin treatment, cross-border recognition and legal certainty must be addressed with industry standards and regulatory clarity. The objective should not be to create an entirely new regulatory framework, but rather to adapt existing rules and standards where necessary to support the safe use of tokenized assets in the derivatives market.

Meanwhile, the prospect of 24/7 trading and clearing is gaining traction for certain asset classes as market participants seek further efficiencies. This would be a huge transition that would require the continuous availability of critical market infrastructure, including middleware and third-party service providers. Systems built for daily processing cycles would need to be adapted to support continuous, real-time operation, making greater automation and straight-through processing essential.

Crucially, 24/7 trading requires 24/7 risk management. Market participants and clearing houses would need to be able to move collateral on a continuous basis, without the bottlenecks and inefficiencies that exist today. As it stands, the most widely used forms of collateral and funding are not reliably available on weekends or holidays. The prospect of tokenized collateral could provide a near-term way to achieve continuous margin movement, supporting the transition to 24/7 trading.

ISDA is well advanced in building the standards, documentation and infrastructure to advance tokenization responsibly and support the transition to 24/7 trading. We're now working with members on a tokenization proof of concept to show how ISDA documentation can be used to exchange tokenized collateral and identify any updates that will be needed to our credit support documentation and supporting legal opinions.

Ten years ago, the launch of the ISDA SIMM resolved a shared industry challenge and brought vital efficiency to the calculation of regulatory IM. A decade later, we're working to deliver further efficiencies by unlocking the potential of tokenization and 24/7 trading.

Scott O'Malia
ISDA Chief Executive Officer

ESMA Sets Out Path to Improve Transaction Reporting

The European Securities and Markets Authority (ESMA) has identified up to €1 billion in potential annual savings from simplified EU transaction reporting as it moves towards a 'report once' approach that it believes would reduce duplication, inconsistency and costs in the reporting framework.

In its final report on EU transaction reporting, published on July 2, ESMA set a long-term objective to remove duplicative reporting, as well as a set of measures to provide more immediate relief, including the expanded use of delegated reporting arrangements and the adjustment of some reporting fields.

"Effective trade reporting that delivers meaningful transparency has been the most elusive of the post-financial crisis reforms, thwarted by duplication, inaccuracies and omissions in reported data. ESMA's vision of a single reporting framework is a huge opportunity to finally develop an efficient EU framework that is less burdensome for market participants and delivers meaningful transparency for supervisors," says Scott O'Malia, chief executive of ISDA.

As it stands, EU market participants may be subject to reporting requirements under three separate regulations – the Markets in Financial Instruments Regulation (MIFIR), the European Market Infrastructure Regulation (EMIR) and the Securities Financing Transactions Regulation (SFTR). ESMA's vision of a report-once approach would move towards a single reporting framework, in which transaction data is only reported once and can be reused across multiple authorities and mandates if required.

Bringing together the reporting requirements from MIFIR, EMIR and SFTR into a single framework will be a major transition. ISDA's Digital Regulatory Reporting (DRR) initiative, which has so far converted industry-agreed interpretations of nine sets of reporting rules into machine-executable code, will continue to evolve to support the implementation of updated reporting rules in the EU and beyond.

Meanwhile, the requirement for both counterparties to report has been a huge operational burden for market participants and a leading cause of cost. ESMA stopped short of a shift to single-sided reporting, proposing instead to expand the use of mandatory delegated reporting under EMIR and the SFTR, in which one party would be solely responsible and legally liable for reporting the trade, but the other would still need to provide that party with certain static data it might not possess.

"If this solution is used, it must be appropriately implemented, with a sufficiently broad scope so the non-reporting entity isn't confined to a small subsection of the market. We must also make sure non-reporting entities aren't required to submit data on a trade-by-trade basis and that trade-repository-level reconciliation requirements are removed. Ultimately, the solution must actually reduce costs, rather than simply shifting them elsewhere," says O'Malia. IQ

To find out more about the ISDA DRR, visit: tinyurl.com/5f7467tx

For more on ESMA's final report, see pages 32-35

ISDA Notices Hub Begins Second Year with Rising Industry Adoption

The ISDA Notices Hub, which enables the near-instantaneous delivery of termination-related notices from anywhere in the world, has seen rising industry adoption as it passed the one-year milestone in July. The ISDA 2025 Notices Hub Protocol, which provides the legal basis for the use of the platform, has now garnered 196 adherents, including global dealers, asset managers, pension and insurance companies, supranationals, corporates, central banks and government bodies.

The Notices Hub, which is available via S&P's Counterparty Manager Platform, was launched in July 2025 to address the risks and costs that arise from delayed or failed delivery and receipt of notices. ISDA estimates firms could save around $1 million if termination becomes effective on a Friday afternoon rather than a Monday morning, even for a modest portfolio of derivatives with $10 million of initial margin.

"Entities that have gone live on the platform have gained potentially vital time advantages versus competitors that continue to rely on physical delivery. Their ability to quickly close out their mark-to-market exposures removes value-at-risk exposure and allows them to re-hedge, set-off and enforce against available security ahead of their peers," says Scott O'Malia, chief executive of ISDA.

The ISDA Notices Hub is already supported by legal opinions in 38 jurisdictions, including all of North America, most of Europe and a high proportion of Asia-Pacific derivatives trading regions. More than 30 jurisdictions are also in the pipeline.

"Anyone doubting the platform's utility only has to consider how difficult physical delivery of a notice would have been during the snowstorms that blanketed eastern America this winter or the events that have played out in the Gulf region since February. The ISDA Notices Hub delivers near instantaneously, regardless of what is happening on the ground, and brings a critical part of the derivatives lifecycle into the 21st century," says O'Malia. IQ

To find out more about the ISDA Notices Hub, visit: tinyurl.com/mr2wv7kj

ISDA and World Bank Group Sign MoU

ISDA and the World Bank Group (WBG) have signed a memorandum of understanding (MoU) to support the development of local derivatives market capabilities in emerging market and developing economies (EMDEs).

The MoU, signed on July 15, establishes a framework for cooperation to support the development of deep, resilient, transparent and internationally connected capital markets in EMDEs, with a particular focus on domestic derivatives markets. This includes working together to promote robust legal, regulatory and institutional foundations, including close-out netting frameworks, derivatives market infrastructure, risk management practices and technical capacity building.

"Derivatives markets are not a nice-to-have – they are an absolutely fundamental component of modern financial markets. They enable risk to be managed rather than avoided, supporting local currency financing and helping banks to manage interest rate and foreign exchange exposures without restricting lending or shortening loan maturities. Vibrant derivatives markets can also improve price discovery and transparency, strengthen market resilience and increase the attractiveness of local markets for domestic and international investors, helping to channel capital into productive economic activity," says Scott O'Malia, ISDA's chief executive.

For many years, ISDA has worked with policymakers and market participants around the world to establish the legal foundations needed for safe and efficient derivatives activity, including close-out netting. However, successful derivatives markets also require appropriate regulation, effective infrastructure, reliable benchmarks, broad participation and strong risk management capabilities. Building technical expertise among local market participants is equally important. These priorities sit at the heart of ISDA's new emerging markets strategy, reflecting a broader focus on market development that goes beyond legal reform to address the full range of conditions needed for safe, liquid and efficient derivatives markets. The MoU with the WBG reflects these shared objectives.

> "Derivatives markets are not a nice-to-have – they are an absolutely fundamental component of modern financial markets"
>
> **Scott O'Malia, ISDA**

"As EMDEs account for a growing share of the global economy, ensuring they have access to a functioning local derivatives market will become increasingly important. But that requires strong legal, regulatory and infrastructure foundations to be in place. Through this partnership, ISDA and the WBG can help more countries build those foundations, deepen local capital markets and realize the benefits that effective risk management can bring to financial stability and economic development," says O'Malia.

S&P Global Selected as Determinations Committee Administrator

ISDA and the Credit Derivatives Governance Committee have announced the selection of S&P Global Market Intelligence as the administrator for the Credit Derivatives Determinations Committees (DCs).

The announcement follows an invitation to tender issued in November 2025. The DC administrator is responsible for various tasks, including acting as DC secretary, building and operating a replacement DC website, and developing and running all infrastructure required to administer the DC process. The administrator will also work with the Credit Derivatives Governance Committee to continue improving the DC rules to meet market expectations for efficiency and transparency in credit event determinations and ensure the long-term viability of the DCs.

"As an independent DC administrator, S&P Global Market Intelligence will work closely with the Credit Derivatives Governance Committee to further enhance the transparency of the DC process and implement agreed structural changes, such as moving towards a non-market-participant decision-making body – steps that will boost confidence in the integrity of the DCs," says Katherine Tew Darras, ISDA's general counsel.

The appointment of an independent DC administrator is the latest in a series of measures to strengthen DC processes and follows publication by ISDA of the results of a consultation on proposed changes to the DCs in 2024. The consultation, conducted by Boston Consulting Group, was based on recommendations proposed by Linklaters as part of an independent review on the composition, functioning, governance and membership of the DCs.

The DCs were introduced in 2009 as a centralized decision-making body to enable a standardized auction settlement process and ensure central clearing could be implemented for credit derivatives. Although ISDA does not control the DC rules and is not involved in the decision-making process or administration of the committees, it has an interest as a global trade association for derivatives in ensuring the DCs continue to function robustly.

In May 2025, ISDA published a proposal for a new governance committee for the DCs, which was established in July 2025. Under ISDA's proposal, the governance committee comprises 15-20 business-focused, decision-making leaders that represent a broad range of participants in the credit default swap market. This includes 10 from the sell side, five from the buy side, three central counterparty or index provider members, and two additional infrastructure providers.

THE COVER PACKAGE

Calibration Test

With Basel III nearing completion, the success of the capital framework depends on risk-sensitive adjustments and consistent implementation

Calibrating capital requirements is a highly complex undertaking and getting it wrong can have serious consequences. Too much lenience might lead to banks holding insufficient capital to mitigate their risks. But excess conservatism can put balance sheets under strain, forcing banks to either raise costs for end users or withdraw from certain businesses, with negative repercussions for the economy.

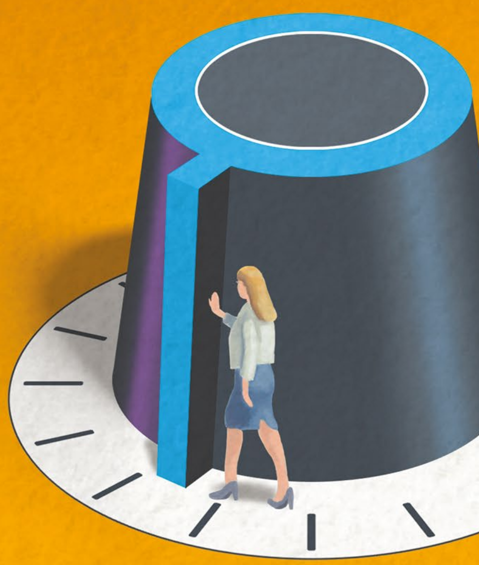
With such high stakes, it's no surprise that the completion of Basel III, which includes new capital requirements for market risk, has occupied so much industry attention in recent years. In the US, the latest Basel III endgame proposal made important progress in improving risk sensitivity, but as ISDA's recent quantitative impact study highlighted, there are still vital adjustments to be made as the rules are finalized. It's also critical that policymakers take a pragmatic approach to implementation, allowing sufficient time for the adoption of internal models (pages 10-13).

For market participants, implementation brings its own set of challenges, including the need to deploy capital models accurately and consistently. ISDA Capital Models Benchmarking has a proven track record in giving banks greater confidence they are using capital models in line with their peers and regulatory expectations. As the European Banking Authority (EBA) prepares to expand its market risk benchmarking exercise next year, ISDA's offering will be available to help newly in-scope banks meet the regulator's requirements (pages 14-17).

With the US, EU and UK progressing towards the Basel III finish line, industry participants are calling for international consistency so that globally active banks can compete on a level playing field. For the EBA, which has set out proposals to improve the efficiency of the regulatory and supervisory framework in the EU, there is a balance to be struck between risk sensitivity, simplicity and the need for a stable and robust banking system (pages 18-21). IQ

"ISDA remains committed to collaborating with global regulators to finalize a capital framework that is both robust and highly risk-sensitive"

Amy Hong, ISDA



* Final Push

As they look to finalize the Basel III endgame proposal, US policymakers should consider the industry's latest recommendations to ensure the capital framework reflects economic risk and doesn't inflict negative consequences on trading and capital markets

Long-distance runners and cyclists are all too familiar with the concept of 'hitting the wall' – the point at which, after a long stretch of continuous exercise, the body runs out of glycogen, one of its main sources of energy. This can lead to severe exhaustion, muscle fatigue and a painful struggle to reach the finish line. Many athletes develop strategies to avoid the dreaded wall, carefully calibrating their intake of high-energy food and drink in the days and hours leading up to a race and pacing themselves in the early stages to ensure they have sufficient reserves for the final stretch.

The development of the Basel III capital framework has been a marathon of its own, spanning many years of drafting, consultations and revisions, and some policymakers might well feel they have hit a kind of wall. In the US, prudential regulators are working to wrap up the Basel III endgame rulebook they first proposed more than three years ago, with a revised draft published earlier this year. But just as successful athletes must maintain focus and stamina to achieve their goals, regulators can't afford to let up at this critical stage. To achieve an appropriate, risk-sensitive capital framework, it is vital that the latest round of industry feedback is fully considered before the US rules are set in stone and a deadline is set for implementation, industry participants argue.

"While the latest US Basel III proposal makes real progress on risk sensitivity, further refinement is needed. As currently drafted, trading book capital requirements remain out of step with economic risks and more conservatively calibrated than international standards. These rules could unnecessarily restrict banks' ability to provide vital market liquidity and hedging services that serve to strengthen the US economy. By adopting the industry's practical recommendations, regulators can deliver a highly risk-sensitive, robust framework with international calibration that supports both financial stability and economic growth," says Amy Hong, chair of ISDA.

In the six months that have passed since US regulators published a new proposal for the Basel III endgame package on March 19, market participants have had the opportunity to scrutinize the details and test the impact of the rules. ISDA conducted a quantitative impact study (QIS) with input from the eight US global systemically important banks (G-SIBs), which informed its response to the consultation that was submitted on June 18.

The QIS showed that the market risk portion of the framework – the Fundamental Review of the Trading Book (FRTB) – would increase capital requirements by roughly 89% if the standardized approach was applied across the full portfolio and by around 30% under a blend of internal models and the standardized approach that reflects current model approvals. This represents a substantial improvement on the original proposal, which would have led to increases in market risk capital of between 73% and 101%. However, the QIS highlighted certain areas where adjustments are still needed to more closely align capital requirements with economic risk.

"The latest QIS clearly highlighted a reduction in risk-weighted assets (RWAs) relative to the previous proposal, but banks would still face an increase in market risk capital requirements, depending on the extent to which internal models are used. By making the final technical adjustments that have been recommended, the agencies can establish a

Illustration: James Fryer

risk-sensitive capital framework that preserves appropriate incentives for market making and risk intermediation," says Panayiotis Dionysopoulos, global head of financial and enterprise risk at ISDA.

> "As currently drafted, trading book capital requirements remain out of step with economic risks and more conservatively calibrated than international standards. These rules could unnecessarily restrict banks' ability to provide vital market liquidity and hedging services that serve to strengthen the US economy"
>
> **Amy Hong, ISDA**

Cross-product netting

One of the principal outstanding concerns relates to the capitalization of counterparty credit risk. Under the new expanded risk-based approach (ERBA), the option to use internal models will be removed for everything except market risk, so US banks will have no choice but to use the standardized approach for counterparty credit risk (SA-CCR) once Basel III comes into effect. With no alternatives available, the calibration of this measure has come into sharp focus.

Under the original proposal, SA-CCR would have required banks to capitalize their derivatives and repos on a product-by-product basis, without being able to net exposures at the portfolio level. While their clients would be able to gain valuable efficiencies from cross-product margining services, such as the one offered by the Fixed Income Clearing Corporation and CME Group, those margin savings would actually cause the capital requirements of bank intermediaries to spike under SA-CCR, constraining their capacity to provide liquidity to the US Treasury market.

Solving this problem has become increasingly urgent as the countdown towards mandatory clearing of US Treasuries intensifies. Under rules introduced by the US Securities and Exchange Commission (SEC), cash Treasury transactions are due to be cleared from the end of this year, followed by repos in mid-2027. Industry →

"Effective cross-product netting is going to be vital for the efficiency of the US Treasury market as mandatory clearing comes into effect"

Benny Crapanzano, Morgan Stanley

participants argue it is critical the SA-CCR methodology is amended so banks aren't faced with disproportionate capital requirements at a time when the provision of client clearing services is vital to the success of the SEC rule.

Following extensive engagement with prudential policymakers since 2023, the latest proposal included an extended SA-CCR framework that would permit the recognition of offsets for certain repo and derivatives trades within qualifying cross-product master netting agreements, including those between clearing members and their clients. This was an important step forward, but the proposed methodology would still lead to disproportionately high capital requirements that don't accurately reflect the economic risk of well-hedged portfolios.

The inherent challenge of cross-product netting lies in the need to recognize the maturity mismatch between typically longer-dated derivatives and shorter-dated repos. To achieve this, the proposal incorporates a simple maturity ratio, but the methodology is calibrated against the gross calculation of derivatives and repo exposures, leading to significant overstatement of risk and limited capital relief, even for fully hedged portfolios.

"Effective cross-product netting is going to be vital for the efficiency of the US Treasury market as mandatory clearing comes into effect. This is something policymakers clearly recognized when they permitted cross-product netting under SA-CCR, but we need to get the methodology right so that banks don't find themselves having to hold so much capital that they can't provide liquidity and clearing services," says Benny Crapanzano, managing director and global co-head of financial resources and strategy at Morgan Stanley.

In its response to the latest consultation, ISDA recommended that a hedge coverage ratio should be incorporated into extended SA-CCR. This would calibrate the netting benefit according to how well the repos in a portfolio actually hedge the derivatives, leading to a more risk-sensitive treatment while also retaining an appropriate level of conservatism. ISDA also recommended the expansion of the positions eligible for extended SA-CCR to include certain margin loans and cleared transactions.

"Extended SA-CCR is an important step towards the recognition of cross-product netting, but the current proposal is not sufficiently aligned with market practice or economic risk. By enabling banks to properly recognize risk offsets in a portfolio of repo and derivatives when calculating capital, consistent with the margin efficiencies they gain from clearing house cross-margining arrangements, regulators can ensure the capital framework supports rather than hinders the transition to Treasury clearing," Dionysopoulos explains.

Targeted adjustments

The calibration of SA-CCR is not the only part of the framework where adjustments are needed. While the QIS showed a reduction in market risk RWAs due to the changes made in the latest proposal, banks would still see a jump in capital requirements for their trading businesses versus the current framework. A substantial share of this impact is driven by the FRTB default risk charge (DRC), which accounts for roughly 51% of market risk capital, according to the QIS.

The proposed rules do not permit the use of internal models to calculate the DRC, so ISDA has recommended a series of adjustments to the standardized approach DRC that would reduce the overall impact of the FRTB and more closely align capital with risk. These include enhanced recognition of equity hedges, exclusion of certain non-US sovereign exposures from the DRC, recalibration of the hedge benefit ratio to better recognize hedging between long and short positions and enhanced recognition of diversification through the introduction of an inter-risk-class correlation parameter.

While the QIS showed market risk RWAs would increase by 89% for the standardized approach as a result of the current proposal, these adjustments would reduce the impact to 44%. For the internal models approach, when the recommended adjustments to the DRC are combined with improvements to the framework for non-modelable risk factors, the RWA impact would fall from 30% to around zero (relative to current requirements).

"These recommended changes to the DRC, which have been informed by quantitative testing and analysis with the G-SIBs, are really critical to ensure market risk capital requirements are fully aligned with economic risk, whether banks opt for the standardized approach or internal models. If capital and risk aren't properly aligned and returns aren't sufficient to offset capital costs, banks will be forced to either scale back from the relevant businesses or raise costs. Neither is good news for end users, particularly as the business lines that will be most affected are those that are critical to financing and hedging," says Lisa Galletta, head of US prudential risk at ISDA.

Beyond the calibration of SA-CCR and the FRTB, ISDA has also recommended changes to the treatment of credit valuation adjustment (CVA) risk under the new framework. Rather than calculating CVA risk for all counterparties in one bucket, which would result in the overstatement of risk for regulated financial entities, ISDA proposes a clearer distinction between regulated and unregulated financial counterparties to deliver a more risk-sensitive outcome. The QIS suggested the capitalization of CVA under the ERBA would result in around $168 billion in RWAs for the eight G-SIBs, but ISDA's recommendations would reduce this impact by roughly 35%.

"Because the CVA charge is fully additive under the proposed framework, any miscalibration flows straight through to capital requirements, with no offsetting mechanism to absorb it. It is therefore important that the framework differentiates more clearly between regulated and non-regulated counterparties, and the threshold at which entities are required to calculate CVA capital is better targeted so it doesn't capture large volumes of derivatives activity that carry no material CVA risk," Galletta explains.

Towards implementation

Taken together, the latest industry recommendations create the opportunity to refine and complete a framework that has already improved significantly, ensuring capital requirements are closely aligned with underlying economic risks. But just as endurance athletes must carefully plan for the final stage of a race, successful regulation depends on a pragmatic and transparent approach to implementation.

Although US policymakers have not yet set a date for implementation of the endgame package, it is vital that the industry is given sufficient time after the rules have been finalized. On the basis that the final rules are expected before the end of this year, ISDA has recommended that the implementation date should be no earlier than January 1, 2028, with an additional 18-month transition period for internal models to mitigate resource constraints and operational burdens for banks and regulators.

While the latest iteration of the framework significantly improves incentives for the use of market risk internal models, banks will be unlikely to use them unless they are given sufficient time to build the necessary expertise, develop the models and secure regulatory approval. An appropriate transition period would also reduce the risk of cliff-edge capital shocks.

"It is encouraging that US policymakers have made positive revisions to the Basel III framework, which included a clear judgment that large trading banks with diversified businesses should be able to use internal models for market risk. It is now essential that a sufficient period of time is allowed for implementation, which is why the industry has proposed the rules should go live no sooner than the start of 2028, with an 18-month transition period for FRTB internal models. As long as the rules are finalized by year-end, this should be a realistic time frame," says Crapanzano.

As US policymakers enter the final stretch towards the completion of the Basel III endgame, industry participants hope they will take due consideration of their latest recommendations, both on the timing and content of the rules.

"ISDA remains committed to collaborating with global regulators to finalize a capital framework that is both robust and highly risk-sensitive. Incorporating these critical technical adjustments will ensure the rules support deep, liquid markets and broader economic growth without compromising the safety and soundness of the global financial system," says ISDA's Hong. IQ

Read ISDA's report on the key findings of the QIS and the principal recommendations to US agencies: tinyurl.com/e679e4u3

UK PRA URGED TO PURSUE GLOBAL CONSISTENCY ON FRTB-IMA

As it considers adjustments to the Basel 3.1 internal model approach (IMA) for market risk, the UK Prudential Regulation Authority (PRA) has been urged to continue pursuing consistency with the US and the EU as both jurisdictions finalize and implement the Fundamental Review of the Trading Book (FRTB).

In a joint response to the PRA consultation on adjustments to the IMA that was due to be submitted as **IQ** went to press, ISDA, the Association for Financial Markets in Europe, the Institute of International Finance and UK Finance welcomed the PRA's proposals and reiterated the need to reduce operational complexity and excess conservatism in the FRTB framework, particularly the IMA.

Based on existing data and feedback from market participants, only a small number of banks plan to adopt the IMA for relatively few desks. The PRA's proposals are designed to improve the proportionality and reduce the operational burden of the IMA framework, which could incentivize greater adoption.

The associations welcome the PRA's proposed adjustments, including changes to the profit-and-loss attribution test, non-modelable risk factors and the risk factor eligibility test, while proposing some additional modifications to further improve the operational functioning of the framework and better align capital requirements with risk.

The PRA has proposed an unchanged implementation date of January 1, 2028 for the IMA, irrespective of any changes resulting from the consultation. However, the associations recommend that some flexibility should be retained to ensure alignment with other jurisdictions, with the option of transitional arrangements that permit firms to continue using the existing IMA where overseas implementation is materially delayed.

Building Confidence

As Basel III implementation enters a new phase, ISDA's Capital Models Benchmarking initiative is evolving to help banks and supervisors understand why the outcomes from capital models sometimes differ, and whether those differences are justified

For all the complexities of the Basel III framework, the original objectives were relatively straightforward. While the first phase of the reforms focused on raising the level and quality of regulatory capital, the second phase, which was finalized by the Basel Committee on Banking Supervision in 2017, sought to restore credibility to the calculation of risk-weighted assets (RWAs) and improve the comparability of banks' capital ratios.

That's far more challenging than it sounds, not only because different jurisdictions interpret global standards in their own way, but also because banks tend to interpret rules independently, particularly when it comes to the models they use to calculate RWAs. Improving the comparability of outputs from those models is far from straightforward. That's why benchmarking has become such a valuable tool to analyze the use of capital models across institutions and jurisdictions, raising confidence in the standardized and internal models that are used for these calculations.

Since its launch in 2018, ISDA Capital Models Benchmarking has enabled banks around the world to achieve a high level of accuracy and consistency in their model implementation, paving the way towards the effective completion of the Basel III framework. But benchmarking is not confined to the banks themselves – supervisors also use it to monitor the use of capital models and identify outliers. In fact, EU supervisors are extending their own benchmarking requirements to a wider pool of banks ahead of the implementation of the Basel III market risk capital requirements in the EU next year, driving the further evolution of this crucial industry practice.

"One of the defining features of Basel III is an overhaul of capital models, with much more stringent approval processes for the use of internal models and more complex, risk-sensitive standardized models. The long-term success of the new framework relies on a commitment to accurate and consistent implementation of those models, which is why benchmarking has become so important. We delivered the right solution at the right time, and we've worked closely with banks to extend it in line with industry practice and supervisory expectations," says Mark Gheerbrant, global head of risk and capital at ISDA.

Benchmarking evolution

In its original iteration, ISDA Capital Models Benchmarking responded to the increasing complexity of standardized capital models for market risk, credit valuation adjustment risk and counterparty credit risk (CCR). As the Basel III framework has been rolled out around the world, it has driven greater use of standard models to capture those risks, with the use of internal models either prohibited or subject to more stringent eligibility tests than in the past.

These standardized models are more sophisticated than previous iterations, requiring banks to allocate substantial amounts of time, resources and expertise to implementation. Benchmarking gives them greater confidence they are implementing consistently and in line with regulatory expectations.

"Benchmarking provides an objective way to distinguish variability arising from genuine differences in risk profiles from variability driven by modeling choices. By comparing results across institutions using common portfolios, supervisors and banks can better understand the material drivers of differences in outcomes, identify areas where modeling practices diverge and assess whether those differences are justified," says Xabier Anduaga, partner in quant services at London Stock Exchange Group (LSEG).

While banks will usually run their own internal validation processes to determine whether a model is conceptually sound, implemented correctly and fit for its intended purpose, that process typically focuses on the most material model components and will only be able to develop a limited number of challenger models or alternative assumptions, Anduaga explains.

"Benchmarking adds an external perspective that cannot easily be replicated internally. It allows firms to compare their modeling approaches and outcomes against those of their peers, providing valuable insight into industry practices. It can also highlight areas that require further investigation and support continuous model improvement," he says.

ISDA's benchmarking initiative comprises two distinct components: an aggregation test and a hypothetical portfolio exercise (HPE). The aggregation test gives banks a prescribed set of input sensitivities and reference data that they run through their model, and the results are then compared to ISDA's golden source results, with any differences flagged for further investigation. Under the HPE, banks conduct the end-to-end capital calculations with a set of hypothetical trades and then submit capital results and input sensitivities into ISDA Analytics, a secure, cloud-based platform that underpins the benchmarking solution. The platform processes the data, presents the results and explains any variance from the median benchmark capital for each portfolio.

Over the past eight years, more than 80 banks have participated in ISDA's benchmarking program, while 15 technology vendors are currently licensing the tests so smaller banks that rely on third-party systems for capital calculations can benefit from benchmarking. Supervisors have also been able to use benchmarking to obtain valuable insights when monitoring the use of capital models by banks in their jurisdictions. The UK Prudential Regulation Authority (PRA) is among a number of regulatory authorities that have been closely associated with the development of benchmarking over the years.

"Model risk management and validation functions are designed to assess and test capital models within a bank's own framework, but what benchmarking delivers is comparability with peers. This enables banks to better understand the impact of various modeling assumptions on exposure, capital calculations and model performance and determine how those compare with other industry approaches. This is very helpful analysis that model validation on its own does not deliver," says Giorgio Donadei, head of Basel risk governance for the UK at Citi.

Extending the benchmark

In the EU, the European Banking Authority (EBA) conducts an annual exercise to assess the consistency and comparability of RWAs across all EU institutions authorized to use internal models. The agency's latest assessment, published in June, highlighted stable and relatively low dispersion for market risk internal models, reflecting improved data quality and convergence in modeling practices.

But this kind of supervisory benchmarking isn't merely procedural – where outliers are identified, it can lead to remediation efforts. As well as analyzing the use of internal models, the EBA also now publishes a separate report on the alternative standardized approach (ASA) under the Basel III market risk framework, known as the Fundamental Review of the Trading Book (FRTB). The latest exercise suggested the ASA had become a more stable and comparable framework, with continued improvements in consistency, but seven banks were flagged for further supervisory review.

For the banks that are required to submit data to the EBA, ISDA runs a shadow benchmarking exercise in parallel. Germany's LBBW, for example, has submitted to the EBA for more than 10 years and has participated in ISDA's shadow benchmarking for the past two years to validate its submissions to the regulator. →

"ISDA has developed unique expertise through our benchmarking of capital models over the past eight years and we have tried-and-tested infrastructure ready for banks to use so they can be sure they are making their best submissions from the first attempt"

Paola Rensi, ISDA

"Model risk management and validation functions are designed to assess and test capital models within a bank's own framework, but what benchmarking delivers is comparability with peers"

Giorgio Donadei, Citi

→ "Being able to do that dry run ahead of the EBA submission has been a very valuable exercise for LBBW, allowing us to address any booking issues in good time and making sure our results are consistent with our peers. This is a complex exercise, and we really see the benefit in being able to validate all the deals, instruments, portfolios and sensitivities that need to be included in our submissions," says a senior risk analyst at LBBW.

For the 2027 exercise, the EBA will expand the scope of market risk benchmarking to a much wider pool of banks that use the ASA, including firms that do not use internal models. While the 2025 exercise covered 43 banks across 13 jurisdictions, the EBA has estimated the expansion in the scope of ASA data collection will increase the pool of banks to roughly 100.

"This is a major expansion in the scope of the EBA's exercise that will require the participation of a large number of banks, many of which may never have done this kind of data-intensive and time-sensitive benchmarking before. Early preparation is vital, as the exercise requires coordination across multiple internal systems and teams, and data needs to be submitted within a fixed timeline," says Paola Rensi, head of ISDA Capital Models Benchmarking.

In a consultation published on July 17, the EBA proposed to postpone the 2027 exercise until the second half of next year, which will give newly in-scope banks additional lead time. As those banks prepare for the exercise, they can leverage ISDA's benchmarking resources, including the ISDA Analytics technology platform, the ISDA EBA Shadow Benchmarking Working Group and ISDA-led training on the analytics platform and the EBA benchmarking process.

"ISDA has developed unique expertise through our benchmarking of capital models over the past eight years and we have tried-and-tested infrastructure ready for banks to use so they can be sure they are making their best submissions from the first attempt. We're pleased to extend our support to those banks that will now fall within the scope of the EBA's extended ASA benchmarking. By using the ISDA Analytics platform and participating in our working group, banks will be able to align themselves with their peers and identify booking, calculation or interpretation issues early on, increasing their own confidence in the submissions they will make next year," Rensi explains.

Even for those banks that have already participated in EBA benchmarking and have the necessary processes in place, next year's expansion will be a major change. For all in-scope entities, the priority is to clearly understand the requirements and start preparations as early as possible, leaning on shared resources like those provided by ISDA where it makes sense to do so.

"Meeting the EBA's benchmarking requirements is a significant undertaking and banks need to act early to understand the process, identify key stakeholders and clearly define roles, responsibilities and accountability. Industry shadow benchmarking exercises help firms to test their processes, address interpretation and implementation challenges with peers and resolve any issues before making formal supervisory submissions," says Paul Glacken, a member of Citi's risk analytics governance team supporting the bank's primary EU banking entity.

Evolving to CCR IMM

While the expansion of the EBA's benchmarking exercise reflects a growing supervisory focus on the use of standardized approaches, ISDA is extending its own benchmarking into one of the most complex parts of risk management – the use of internal models for CCR. The internal model method (IMM) for CCR is less prescriptive than other modeling techniques and risk types, which has resulted in a wide range of approaches across the industry. Banks see this as the most challenging phase of the benchmarking journey so far.

"For the FRTB standardized approach and even for current and future market risk internal model approaches, regulatory requirements tend to be more prescriptive. This results in a generally good alignment across peers and the benchmarking evidencing robust comparability, but for CCR IMM models, that's not the case. The IMM framework has additional complexities, forcing the requirements to be less prescriptive, ultimately leading to greater variability across banks, which makes an industry benchmarking framework very helpful," says Citi's Donadei.

"The IMM is typically implemented using Monte Carlo simulation, so a single headline metric such as capital or exposure offers limited diagnostic value when attempting to explain discrepancies between firms – such metrics describe the result, but reveal little about the drivers behind that result. In practice, differences in outcomes can stem from multiple modeling components, but without sufficiently granular and comparable diagnostic data, it is difficult to attribute differences to specific modeling elements, which in turn makes peer comparison of IMM outcomes difficult," says Öykün Altug-Polikar, head of CCR and XVA model monitoring development at HSBC.

ISDA's framework for the benchmarking of CCR internal models, which was published in May, is designed to achieve comparability of outcomes across banks, ensuring assessments are based on a broad set of outputs, sensitivities and distributional characteristics. The framework also focuses on transparency and interpretability of results, robust validation and verification, the ability to evolve to accommodate future developments and the automation of infrastructure and processes. The design aims for the analysis to be actionable, with conclusions that provide practical insights to inform firms and supervisors.

The framework itself consists of three complementary components: an industry working group that provides input into the design and execution of the benchmarking process; a qualitative survey devised by the working group to understand model implementation features and assumptions; and a quantitative benchmarking process that includes the HPE. As well as allowing for the benchmarking of well-understood counterparty exposure metrics, the HPE also supports the increased complexity of risk factors, payoffs and portfolio features.

Following publication of the framework, ISDA convened an industry workshop involving 10 banks and the PRA to launch a CCR IMM benchmarking exercise aimed at generating transparent and explainable outcomes, improving the identification and interpretation of outliers and enhancing understanding of the drivers of variation in exposure metrics. While impetus for the project has been driven by the PRA and UK banks, some EU banks are also now participating on a voluntary basis as benchmarking of the IMM gains traction.

"ISDA's benchmarking framework for CCR IMM is an important milestone for the industry that provides the foundations for comparing internal model outcomes and reflects valuable lessons learned from the initial benchmarking exercises. The next challenge is to simplify the operational component through automation so participating institutions can adopt the framework consistently and efficiently. Standardizing data inputs, ensuring high-quality reference portfolios and maintaining transparent governance will all be important to achieving repeatable and meaningful comparisons," says LSEG's Anduaga. IQ

BENCHMARKING DOWN UNDER

When it comes to completion of the Basel III framework, recent attention has focused mainly on three major Basel Committee member jurisdictions – the US, the EU and the UK – where the rules have already been finalized or are in the process of being finalized. In Australia, however, a longer time frame has been set out, with the Australian Prudential Regulation Authority (APRA) planning to consult next year on a simplified version of the Fundamental Review of the Trading Book (FRTB), tailored to the specificities of the Australian market.

That doesn't mean Australian banks have been sitting on their hands, however. Earlier this year, ISDA completed an FRTB standardized approach benchmarking project with five Australian banks – ANZ, Commonwealth Bank of Australia, Macquarie, National Australia Bank and Westpac – and direct engagement with APRA. As it begins informal supervisory engagement with banks and prepares to consult on the FRTB next year, APRA has indicated it will draw on the results of the ISDA exercise to inform the process.

"The Australian banks are in a unique position compared to other jurisdictions in that the FRTB rules are still evolving, so ISDA's benchmarking exercise provided a structured opportunity to test the emerging FRTB standardized approach frameworks, complementing existing implementation work by providing tangible calculations and governance discussions in a benchmarking context. They were able to identify implementation differences and areas for further analysis that may have been difficult to observe through internal testing alone," says Paola Rensi, head of ISDA Capital Models Benchmarking.

In applying the benchmarking process to the Australian market, ISDA designed tailored hypothetical trades to ensure the findings would be authentic and relevant. The final results showed a low proportion of outliers, reflecting a high degree of internal scrutiny and validation by the participating banks. APRA's engagement gave the project additional credibility and provided useful insights into implementation approaches ahead of its planned consultation.

"The exercise gave APRA greater confidence in the quality and consistency of FRTB standardized capital models. At a time when APRA is not yet in a position to provide formal policy guidance on the new framework, the banks' participation in ISDA's benchmarking exercise allowed them to remain operationally engaged and proactive in working with the regulator," says Rensi.

* Efficient Regulation

*From the preservation of internal models under Basel III to the calibration of margin requirements, a pragmatic approach is needed to build a more efficient regulatory framework, explains **Lars Overby**, head of risk-based metrics at the European Banking Authority*

IQ: The European Banking Authority (EBA) has set out proposals for a more efficient regulatory and supervisory framework in the EU as part of a broader move towards simplification and efficiency. How is this progressing? Could the existing rulemaking process and the roles of the main EU institutions be streamlined and improved?

Lars Overby (LO): The EBA published a report last October that set out 21 concrete measures, including measures to lower the reporting burden, developing proportionality measures for small and non-complex banks, reviewing the credit risk framework and shifting the EBA's work towards supervisory convergence. We are continuously delivering on these mandates, which can be followed on our website as and when progress is made. The EBA is therefore resolute in its commitment to the political shift, as we all agree that it is good to take a hard look at areas that require improvement.

That being said, and as others have echoed, simplification of the regulatory and supervisory framework is a complex task. Therefore, the work has to be taken step by step. Our aim has to be modest. A first step would therefore be the efficiency of the regulatory framework. There is a reason why the framework looks the way it does today – the world is complex and the rules simply reflect this complexity. If we want a risk-sensitive framework, that also entails more complexity in the rules.

Ultimately, it is about finding a balance between elements such as risk sensitivity, simplicity and the need for a stable and robust banking system. The rulemaking process in the EU is one example – it is clearly very complex, as it allows all to have a say in the process. On some more technical aspects, such as the Fundamental Review of the Trading Book (FRTB) and margin requirements, I find that more can be moved to supervisory processes or Level 2, but, ultimately, this is a more political choice about how to balance the need for technical expertise and, at the same time, ensure a democratic process that respects the framework we have in the EU.

"A level playing field is clearly needed, both to ensure that banks can compete on equal terms, but also to ensure the prudential framework reflects the risks in a comparable manner, so investors can meaningfully assess the risks of banks"

IQ: As US regulators move to finalize the Basel III endgame package and the UK Prudential Regulation Authority consults on adjustments to the internal models approach (IMA) for market risk, the European Commission (EC) has adopted temporary adjustments to the FRTB that will apply for three years from the start of 2027. Do you think these adjustments will have the intended effect of addressing competitive distortions with other jurisdictions, and are you confident there will be sufficient long-term alignment to achieve a level playing field?

LO: The short answer is yes – a level playing field is clearly needed, both to ensure that banks can compete on equal terms, but also to ensure the prudential framework reflects the risks in a comparable manner, so investors can meaningfully assess the risks of banks.

The long answer is that it will be a long road to get there, with even a few bumps along the way. Key jurisdictions all have their own legislative processes to follow and there are quite diverse views around the table, be it in the industry or among supervisors and regulators.

The difficulty will be in building a consensus on the changes that are needed, especially to improve the incentives for use of the IMA. The EBA is working actively on identifying such changes, and we are obviously keeping an eye on any developments outside Europe, but also actively talking, both bilaterally and at the Basel Committee table, to our counterparts. The challenge will therefore be to pin down what changes are needed.

IQ: The latest proposal for the US Basel III endgame made the use of internal models for market risk a more viable option for US banks, while the UK has also proposed changes to the IMA framework. How important is it that internal models continue to be used? Should changes be made to the output floor in the EU to make this more likely?

LO: The EBA has always been a strong proponent of internal models for credit and market risk and that continues to be the case. The EU still has a more 'bank-centric' model, where banks play a key role in providing support to the real economy, as compared to the US model of relying more directly on capital markets funding, also for corporates. Having a risk-sensitive approach – ie, the internal ratings-based approach and the IMA – therefore makes sense in Europe, as it should in theory lead to more efficient capital allocation when the prudential framework reflects the risk of the customers more accurately.

The lack of IMA adoption is therefore something the EBA is looking into. We are now taking stock of the market risk framework and the lack of incentives to adopt internal models. We aim to publish a report by the end of this year or early next year on these issues. That will undoubtedly require changes to the IMA, and the EC delegated act has already pointed to the direction on some aspects. The incentive to adopt is, however, clearly linked to the design of the output floor. Hence, changes to the design of the output floor clearly need to be considered. We are therefore going into this debate with an open mind.

IQ: ISDA has invested in capital models benchmarking over the past eight years, with the aim of helping banks achieve greater accuracy and consistency in their use of capital models, starting with standardized models and evolving to include internal models. As the focus shifts from Basel III rulemaking to implementation, how important is it to benchmark capital models to ensure alignment across the industry? How would you like to see benchmarking initiatives evolve?

LO: The EBA has been doing benchmarking of internal models since 2014 and has worked closely with ISDA, especially on market risk models, since it started its own benchmarking work. It was one of the key measures that the EBA undertook early on to restore trust in internal

"We are now taking stock of the market risk framework and the lack of incentives to adopt internal models. We aim to publish a report by the end of this year or early next year on these issues. That will undoubtedly require changes to the IMA, and the EC delegated act has already pointed to the direction on some aspects"

→ models. I am therefore very supportive of the efforts undertaken by ISDA and the industry in general.

I should also stress that I am a strong believer in market discipline and providing benchmarks to banks and the wider public gives transparency on the use of internal models. It gives banks a tool to identify weaknesses in their own approaches, while also giving supervisors a tool to identify the areas where a bank might be lagging behind its peers. I therefore see this as a key part of the framework for internal models that we have built since the crisis. At the same time, it is not the alpha and omega of modeling and supervision. While it is a valuable tool, it cannot replace sound judgment and robust validation, nor should it be seen as a definitive measure of model quality. I would even say that some diversity in modeling outcomes can help mitigate model risk and herd behavior.

Going forward, it is clear that modeling practices continue to develop. The adoption of artificial intelligence (AI) is probably the clearest example, as this will have clear consequences in the risk management of banks. We will have to consider how to use AI in the benchmarking process – for instance, in data quality processes – but also how AI is used by banks in the model space.

IQ: When it comes to non-cleared margin requirements, the EU is currently an outlier in requiring the retention of initial margin (IM) for previously margined trades after a counterparty falls below the average aggregate notional amount of non-cleared derivatives threshold. How is this issue, which puts smaller EU counterparties at a competitive disadvantage, being addressed?

LO: We have historically been a bit more conservative on this aspect, partly because we have not had the same checks on the use of the IM models that other jurisdictions have. The most important argument has, however, been a more procedural one – that the political negotiations on the European Market Infrastructure Regulation (EMIR) had to be concluded before we could revisit this issue.

With EMIR concluding last year and the EBA taking over the supervision of IM model validation, this has been a natural time to take stock of this particular issue. With the key argument that global convergence is clearly preferable on these more technical aspects, the EBA – jointly with the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority – has chosen to align on this aspect. Hence, we have chosen to listen to the industry request on this issue and recently published an amendment to the EU framework (see box).

IQ: This year marks 10 years since the launch of the ISDA Standard Initial Margin Model (ISDA SIMM) and the EBA is expected to complete its assessment for the validation of the model by the end of this year. What role has the ISDA SIMM played in the efficient rollout of the non-cleared margin rules and the ongoing daily exchange of margin? Do you anticipate any issues with the validation process, or the subsequent process for EU counterparties to obtain authorization from competent authorities?

LO: I chaired the joint EBA-ESMA working group that implemented the margin framework for non-cleared derivatives in the EU in 2012-2015, when we put down the requirements for this. It was clear then that there was a lot of system development and processes that had to be put in place.

Looking back, I am very happy with what has been set in place. I see this as a good example of where we on the regulatory side have put in place requirements. These have been modified over time when issues arose, but the industry took responsibility for implementing the ISDA SIMM. That has been key in solving the coordination problem between counterparties, which is at the heart of the margin framework. Hence, in some sense, the EBA task on validation of the ISDA model is a natural continuation of this work.

On the challenges or issues with the validation process, the EBA is generally taking a pragmatic stance. The framework is generally working well, so we clearly have this in mind as part of our work, as disruption to the market would be detrimental to what has been built.

At the same time, we will have to look at the technical details. We know the US has restricted the use of the ISDA SIMM for some types of derivatives. We will have to look at documentation for the model and we need to understand the market usage and the consequences. Overall, I am confident that we will find a positive outcome on the functioning of the ISDA SIMM, as it has worked well so far.

IQ: The use of digital assets in financial markets is evolving fast and one particular opportunity is the use of tokenization to bring greater efficiency and flexibility to collateral management. What do you see as the most compelling use cases for digital assets, and what challenges need to be overcome?

LO: It is too early to tell how the technology will be used. It is clear that the use of tokenized assets for trading purposes is dominating the headlines. This brings challenges, as the creation of new assets also comes with new risks – although the market naturally focuses more on new opportunities – as the trading characteristics differ from existing assets.

As a regulator, you want to see the performance of an asset through a full economic cycle, enabling us to assess a situation when liquidity grows scarce in a market. The prudential framework consequently tends to be more on the conservative side when we have not seen how assets fare in an economic downturn. But, at the same time, we also have to take care that we embrace new innovations, as things will just move outside the banking system if there is demand, and this will not necessarily reduce overall risk in the system.

On the use cases, it is clear the technology can generally be used to speed up settlement processes, which will be good for collateral management. Having speedier settlement is a good thing and if the new technology can help with this, these will be interesting use cases.

IQ: What will be at the top of your agenda for the rest of 2026?

LO: It is clear that the simplification work, especially related to credit risk and considerations on proportionality measures for small and non-complex banks, will remain high on the agenda. This will hopefully feed into the EC's broader work on simplification, as its competitiveness report, which was published in July, sets the tone for the EU's future work in this area. On issues that relate directly to ISDA's own work, it is clear that finding a way forward on the FRTB, especially on IMA adoption, and implementation of the EBA approach on the validation work on the ISDA SIMM are very high on my list. IQ

EUROPEAN SUPERVISORY AUTHORITIES PROPOSE MARGIN RELIEF FOR PARTIES BELOW THRESHOLD

On August 3, the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority published a final report on draft regulatory technical standards (RTS), proposing to simplify margin requirements under the European Market Infrastructure Regulation (EMIR).

The proposed amendments aim to simplify the bilateral margin framework for counterparties that are subject to initial margin (IM) requirements and that are below the €8 billion threshold for exchanging IM under EMIR. The changes are intended to facilitate the phasing out of IM requirements for these counterparties. They also support greater consistency with the treatment applied in other jurisdictions.

Under the current framework, counterparties that are below the threshold are exempt from exchanging IM for new non-cleared over-the counter derivatives contracts, but continue to exchange IM for existing contracts. With the proposed amendments, counterparties would no longer be required to exchange IM for either new or existing contracts if they are below the threshold.

The amendments respond to requests from market participants and support the broader objectives of simplification and burden reduction.

The final report has been submitted to the European Commission (EC) together with the draft RTS for endorsement. Following the EC's review and adoption process, the RTS will be subject to scrutiny by the European Parliament and the Council of the European Union before being published in the Official Journal of the European Union.

Read the full announcement and report: shorturl.at/pUTz4

The Value of SIMM-plicity

Ten years on from the launch of the ISDA SIMM, the model has become the industry standard for calculating initial margin requirements for non-cleared derivatives, having been adopted by buy- and sell-side institutions around the globe

Risk models are a dime a dozen in financial markets. Institutions might use an array of proprietary tools to calculate and manage risk, with methodologies that remain largely out of public sight. In contrast, standardized regulatory models are fully transparent but tend to be static and are rarely updated, even if market conditions radically change. The ISDA Standard Initial Margin Model (ISDA SIMM) breaks the mold on both counts.

Launched 10 years ago to support the implementation of mandatory initial margin (IM) requirements for non-cleared derivatives, the ISDA SIMM was developed with transparency at its heart. Its methodology is publicly available and subject to a rigorous governance process, its performance is continually monitored and enhancements are driven by quantitative analysis, industry engagement and ongoing dialogue with supervisors. A community of global regulators reviews the model's calibration, backtesting and maintenance, helping to ensure it remains aligned with both market realities and regulatory expectations. This combination of transparency and oversight has helped to establish the ISDA SIMM as a trusted global standard, used by hundreds of buy- and sell-side firms around the world.

Crucially, the ISDA SIMM is a living model. Since its launch in 2016, it has been regularly recalibrated and enhanced to reflect changing market conditions, new products and evolving risk dynamics. More recently, the model moved to a semiannual calibration cycle, enabling it to incorporate new market information more quickly while maintaining a robust governance and review process. The result is a model that continues to evolve alongside the markets it serves – enabling it to successfully navigate periods of extreme market stress, geopolitical uncertainty and structural changes in derivatives markets.

"The ISDA SIMM was an unprecedented response to a major collective challenge for market participants. Over its 10-year history, it has remained robust through multiple market shocks, continuing to provide a risk-sensitive and globally consistent framework for calculating IM. As it enters its second decade, the ISDA SIMM continues to meet the needs of the non-cleared derivatives market, while being reshaped by new products, additional jurisdictions and a growing population of firms coming into scope," says Scott O'Malia, ISDA's chief executive.

Transparency is key

When preparing for the first phase of implementation of IM requirements for non-cleared derivatives in September 2016, industry participants faced a unique problem: both counterparties would have to agree on the amount of IM that would need to be exchanged. Firms could opt to use a conservative standardized schedule developed by regulators or a more risk-sensitive internal model that better reflects the actual characteristics of the underlying trades. But having each entity develop its own proprietary model simply wouldn't work – no one would be able to agree on the amounts calculated, resulting in disputes and delays.

"The unique thing about IM is that you're calculating a figure that has to be paid to you by your counterparty, rather than modeling an amount of capital that will sit on your own book. If you call a counterparty for a certain amount of IM, they naturally want to be sure whether it's reasonable or not," says Scott Cogswell, a regulatory and risk analyst at HSBC.

That called for something unprecedented: a common framework capable of delivering consistent, risk-sensitive margin calculations across the market. "To avoid endless calculation delays and disputes, we realized we'd need to park our egos and cooperate," Cogswell adds.

The result was the ISDA SIMM – a single, industry-wide model that could deliver the risk sensitivity of an internal model, while providing the simplicity and consistency needed for counterparties around the world to agree margin amounts quickly and efficiently.

Unlike many risk models, the ISDA SIMM is fully transparent and designed to be implemented by a broad range of market participants (see box). Its methodology, assumptions and calibration framework are publicly available and can be independently reviewed by market participants, regulators, vendors and service providers. Firms do not need to accept a 'black box' calculation produced by another institution – they can see exactly how the model works and how margin requirements are determined.

An evolving model

However, transparency alone is not enough. Markets evolve, new products emerge and periods of stress can expose new risks. A model that remains static eventually becomes less representative of the market it is designed to measure.

That's why the ISDA SIMM was built with governance and continuous development at its core.

The ISDA SIMM operates under a formal governance framework overseen by the ISDA SIMM Governance Forum and Executive Committee, which coordinate ongoing monitoring, development and maintenance of the model. Proposed changes are supported by quantitative evidence, assessed through extensive analysis and industry consultation and scrutinized through a structured approval process before implementation.

Recalibration is a critical part of that framework. Following coordination with global regulators, the ISDA SIMM moved to a semiannual calibration cycle in 2025, enabling the model to respond more quickly to evolving market conditions while maintaining predictability and operational certainty for users. Under this process, a primary calibration assesses all ISDA SIMM parameters, while a secondary calibration focuses on the main delta risk weights and related parameters.

> "The basic structure of the model remains pretty similar to the structure on day one of implementation, which is a testament to the foresight of the committee that created it. It has withstood a lot of seismic events in the market, without being unduly procyclical and with a very good record on calculation errors and disputes"
>
> **John Pucciarelli, LSEG**

Those reviews are complemented by annual backtesting and benchmarking exercises and quarterly assessments of monitoring data submitted by market participants. ISDA SIMM users are expected to resolve remediation threshold breaches on a bilateral basis within 40 business days, in line with the ISDA SIMM Governance Framework and Remediation Annex. Where evidence points to material and widespread performance issues, those findings are investigated and, if necessary, addressed through model enhancements or recalibration.

Much of this work is supported by ISDA Analytics, a secure web-based platform used by banks, supervisors and ISDA to streamline key aspects of ISDA SIMM monitoring and maintenance. By standardizing data submission, validation and analysis, the platform helps to support the backtesting, benchmarking and monitoring processes that underpin the model's ongoing governance and development.

Importantly, this process operates under the constant gaze of supervisory agencies. ISDA shares detailed calibration, backtesting and performance-monitoring information with a community of global regulators and engages in regular dialogue on the maintenance and evolution of the model. The ISDA SIMM is also subject to a root-and-branch independent validation by an external auditor every three years, providing an additional layer of assurance over the model's soundness and performance.

"The relationship between the industry and regulators has never been completely adversarial but we've also never seen the sort of close cooperation between the two on a global scale that marked the development of the ISDA SIMM. It was amazing to see doors completely open on both sides, with a willingness from all participants to make this work in the interests of the market," says John Pucciarelli, head of partnerships and director of industry engagement for post-trade solutions at the London Stock Exchange Group (LSEG).

Today, more than 440 groups of entities are licensed to use the ISDA SIMM, while 70 vendors are able to provide ISDA SIMM services, including IM calculation, data exchange and backtesting and benchmarking.

"The use of the ISDA SIMM is a ticket to full participation in the global non-cleared derivatives market, which remains a critical risk management tool for thousands of counterparties. Use of a single, transparent model across the industry ensures consistency and lowers the risk of disputes, ensuring margin amounts →

→ can be agreed and posted quickly, reducing delays and mitigating counterparty credit risk," says Nnamdi Okaeme, ISDA's head of SIMM.

Tested in stress

In its 10-year history, the model has seen some of the most volatile periods in living memory – the 2020 pandemic, the opening salvoes of the Russo-Ukrainian war in 2022 and the collapse of Credit Suisse and ensuing banking sector weakness in 2023 – and come through unscathed.

"The basic structure of the model remains pretty similar to the structure on day one of implementation, which is a testament to the foresight of the committee that created it," says LSEG's Pucciarelli. "It has withstood a lot of seismic events in the market, without being unduly procyclical and with a very good record on calculation errors and disputes. When I think back to 2014 or 2015, there was perhaps some doubt as to whether the ISDA SIMM was even possible, and certainly whether it would be ready in time. If you had offered the outcome we have today to the designers back then, they'd have happily taken it, I'm sure."

In those 10 years, modifications have been made outside of those implemented as part of the recalibration process to reflect market changes and regulatory requests. For example, additional risk factors relating to cross-currency swaps, inflation options and collateralized debt obligation tranches were added to the model in April 2017 in response to feedback from US regulators. Further changes may be made in future, including modifications to how currencies are bucketed by risk.

"The ISDA SIMM's currency classification framework has historically combined expert judgment with quantitative analysis and has performed well over time. As the framework evolved, a broader review highlighted the benefits of applying a consistent data-driven methodology across both the interest rates and FX risk classes. ISDA has therefore requested permission to use a more data-driven method for evaluating currency volatility," explains ISDA's Okaeme.

Amid these changes and challenges, the cooperative spirit that created the ISDA SIMM will continue to be evident as the model further evolves.

"There are half a dozen or so of the original committee members still involved in the day-to-day management of the ISDA SIMM," says Eduardo Epperlein, senior technical advisor at Nomura in London. "We don't have to turn up to every call but we generally do. I suppose we feel that in helping the industry make sure the model continues to work, we're doing something good overall. I don't think any of us have been particularly surprised by its success because we were confident in the concept." IQ

The latest version of the ISDA SIMM – Version 2.8+2512 – was published in June 2026 and is available here: tinyurl.com/ycx8dfy4

More information on the ISDA SIMM Governance Framework is available here: tinyurl.com/mry2e92m

NOT LETTING THE PERFECT BE THE ENEMY OF THE GOOD

The ISDA Standard Initial Margin Model (ISDA SIMM) represented a radical departure from the way that industry participants usually go about their business. Capital and risk modeling is a matter for an individual firm and its regulator, not an opportunity for cooperation and consensus. However, when faced with mandatory margin requirements for non-cleared derivatives, firms had to quickly shed traditional attitudes and work with ISDA to develop a standard, industry-wide, risk-sensitive model that could be used consistently around the globe.

Rather than build an entirely new framework from scratch, the decision was taken to adapt a model proposed under revised market risk capital standards, known as the Fundamental Review of the Trading Book. This met the regulatory requirement for IM to cover changes in the value of a portfolio over a 10-day period with a 99% confidence interval, while retaining the transparency and regulatory credibility of an established methodology. The resulting model uses a sensitivity-based approach that is transparent, straightforward to implement and capable of being independently verified by counterparties.

It also resulted in a relatively conservative output, with calculated margin amounts generally higher than would be the case with a more complex model. Ultimately, it was decided that a relatively simple model would lead to the broadest possible adoption, enabling the industry to quickly agree margin amounts with the widest universe of derivatives users. That simplicity was also intended to support efficient dispute resolution and reduce operational complexity by ensuring margin calculations could be replicated and checked across firms.

"If we made the model too exact and too risk sensitive, every user would have needed to build an enormous control function to monitor it. This is what happens with capital models. They require a lot of monitoring because they try to be as close as possible to the right number. By making the ISDA SIMM more conservative, we can monitor and backtest on a fairly lean basis," says Eduardo Epperlein, senior technical advisor at Nomura in London.

For users, that means significant savings in personnel costs and less time and resources spent on margin remediation with counterparties. "If you were to quantify the burden of a more risk-sensitive model against the cost of financing extra margin in the more conservative SIMM, I think it would be a good trade-off for the latter," says Epperlein.

Importantly, the decision to prioritize simplicity did not come at the expense of robustness. The ISDA SIMM operates under a formal governance framework that includes ongoing performance monitoring, backtesting, benchmarking, independent validation and semiannual recalibration. This allows the model to remain both practical to implement and responsive to changing market conditions.

10 Lessons from 10 Years

The first decade of the ISDA SIMM shows how an effective industry solution can evolve from an ambitious concept to a critical part of the market structure. ***Nnamdi Okaeme****, ISDA's head of SIMM, reflects on the model's first decade and what the future might hold*

The introduction of mandatory initial margin (IM) requirements for non-cleared derivatives represents one of the most significant reforms in the post-financial-crisis regulatory landscape. In response to the global framework drafted by the Basel Committee on Banking Supervision and the International Organization of Securities Commissions, ISDA collaborated with market participants to develop the ISDA Standard Initial Margin Model (ISDA SIMM), a transparent and risk-sensitive methodology for the calculation of IM.

Launched in 2016, the ISDA SIMM was designed to support quick and consistent IM calculations, promote timely dispute resolution and reduce fragmentation across jurisdictions. Ten years on, it has become a core pillar of the global derivatives market. The model is subject to semiannual calibration, rigorous backtesting and ongoing review by global regulators. It is supported by one of the most comprehensive collaborative governance frameworks in the industry, incorporating evidence-based analysis and wide-ranging input from banks, asset managers, custodians, vendors and other stakeholders.

At the end of 2025, leading derivatives market participants subject to the margin rules had collected $428.8 billion of regulatory IM, according to the ISDA Margin Survey. At that point, 437 licensed entities and 67 service providers were using the ISDA SIMM to calculate IM, demonstrating its broad adoption, operational resilience and effectiveness as a global standard. The first decade of ISDA SIMM provides a strong foundation for its future. The insights drawn from its evolution point to a model that will continue to uphold its core principles while embracing innovations required for an increasingly digital, interconnected and complex financial system.

Ten specific lessons can be drawn from the first decade of the ISDA SIMM, including the benefits of sustained collaboration and engagement, as well as the key design principles that were needed. Looking to the future, there are opportunities to build on this foundation to accelerate future innovation.

ISDA as a Solutions Incubator

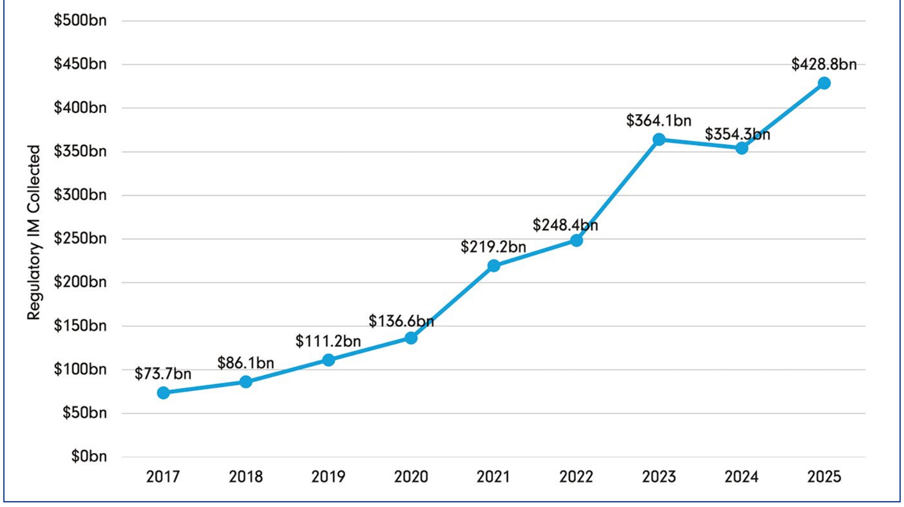
1. ISDA provides a trusted, neutral forum for industry collaboration

The ISDA SIMM demonstrates that complex, system-wide challenges can be addressed very effectively when the industry has access to a well-understood, respected and neutral forum for collaboration. ISDA's convening role provided the space for firms with differing business models and incentives to engage constructively, test ideas and align on a collective plan. This neutral setting was essential to enabling open dialogue, reducing fragmentation and building confidence that outcomes reflected broad market interests rather than those of any single institution.

2. ISDA enables pragmatic consensus building that drives scalable solutions

The success of the ISDA SIMM underscores the importance of balancing technical →

FIGURE 1: TOTAL AMOUNT OF IM COLLECTED, 2017-2025



Source: ISDA Margin Survey Year-end 2025

→ perfection with practical implementation. ISDA's structured governance and voting processes allowed ideas to be iteratively refined, stress tested and legitimized through industry consensus. While compromises were sometimes needed, this pragmatic approach ensured solutions were sufficiently robust to meet regulatory expectations while remaining operationally feasible for widespread adoption. This ultimately supported the scale, durability and global acceptance of the ISDA SIMM.

A critical enabler of this consensus was the shared nature of the regulatory obligation. Firms faced the same mandatory IM requirements on similar timelines, and the ISDA SIMM allowed the industry to centralize a substantial portion of the modeling, calibration, validation and regulatory engagement effort. This avoided large-scale duplication across firms and enabled a form of structured burden sharing, where the costs and complexity of complying with a new regulation were mutualized rather than being borne individually.

3. The ISDA SIMM provides a proven governance template for industry-standard models

The long-term success of the ISDA SIMM demonstrates that robust and transparent governance is invaluable for the credibility and durability of industry-standard models. The governance framework established for the ISDA SIMM now serves as a reusable template for other industry solutions, providing clarity on decision making, accountability, escalation and change management across the model lifecycle.

4. Robust governance requires continuous stakeholder engagement

Effective steady-state governance depends on active and ongoing engagement with stakeholders. The ISDA SIMM shows that regular consultation, structured feedback and inclusive participation across market participants are critical to maintaining trust, legitimacy and alignment as market conditions, regulation and risk profiles evolve.

5. Sustained analytical capability underpins long-term model integrity

Maintaining an industry-standard model requires ongoing quantitative analysis and evidence-based decision making. The ISDA SIMM's steady-state operation highlights the importance of dedicated analytical capability to support recalibration, backtesting, sensitivity analysis and impact assessment. Elements of these design principles, particularly relating to data standardization and evidence-based analysis, have informed other ISDA initiatives, reinforcing consistency and efficiency across industry solutions.

ISDA SIMM Design Principles

The long-term success of the ISDA SIMM is rooted in a set of design principles that supported scale, adoption and operational resilience.

6. The ISDA SIMM was designed for scalability

The first decade of the ISDA SIMM demonstrates how an initiative can evolve into critical market infrastructure. When IM requirements for non-cleared derivatives were first introduced in 2016, they applied only to the largest dealers, and the number of trades in scope was a fraction of the overall market. Over time, both participation and scale increased significantly as the margin rules were progressively phased in and use of the ISDA SIMM broadened. Key to its adoption was a determination that the ISDA SIMM should handle almost all asset classes and derivatives products, ease and speed of calculation and calculation transparency.

7. The ISDA SIMM was designed with a focus on pragmatism over perfection

The success of the ISDA SIMM reflects a deliberate focus on pragmatism rather than theoretical perfection. The model was designed to be sufficiently risk sensitive to meet regulatory objectives while remaining transparent, explainable and operationally feasible at scale.

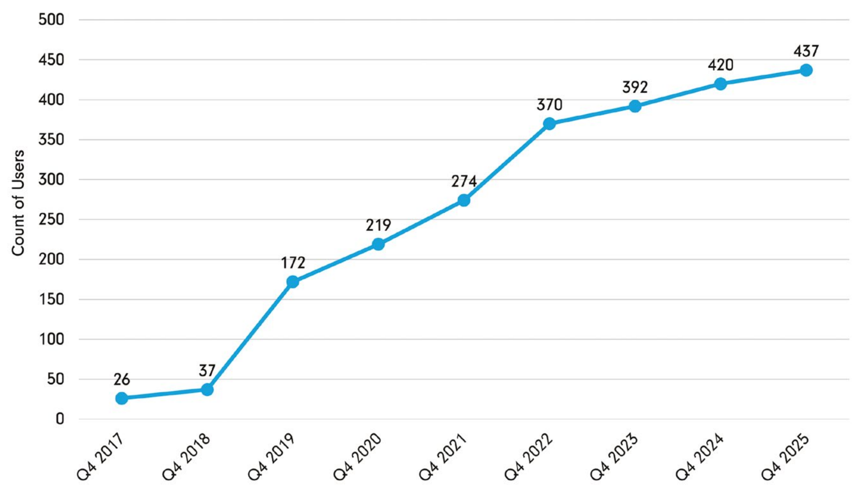
By prioritizing standardized inputs, well-understood risk measures and repeatable calculation steps, the ISDA SIMM enabled consistent implementation across a diverse global user base and avoided the complexity that often undermines adoption of industry models.

This pragmatic approach allowed the ISDA SIMM to be delivered within regulatory timelines, refined through experience and enhanced over time. This demonstrates that durable industry standards are built through practical design choices that balance risk accuracy with usability and governance.

Future Opportunities

The ISDA SIMM has evolved into a trusted industry standard for measuring risk-appropriate IM, providing a single, coherent metric that captures the overall risk of a derivatives portfolio. This foundation creates a number of opportunities that can be explored to leverage the model's design, infrastructure and governance more broadly across the market.

FIGURE 2: ISDA SIMM USER BASE, 2017-2025



Source: ISDA

8. Enhance existing ISDA SIMM collateral infrastructure for faster IM settlement

The ISDA SIMM's role as a single, trusted measure of portfolio risk removed the need for counterparties to reconcile two separate risk-based calculations. Without a common model, parties would have struggled to understand, challenge or resolve differences in margin calls, particularly given the lack of model transparency.

This standardization creates a clear opportunity to streamline collateral infrastructure, enabling faster, more automated and more predictable IM settlement for bilateral relationships across the market. This includes the use of tokenized collateral to support near real-time settlement, which has the potential to reduce the period during which uncollateralized exposures can accumulate.

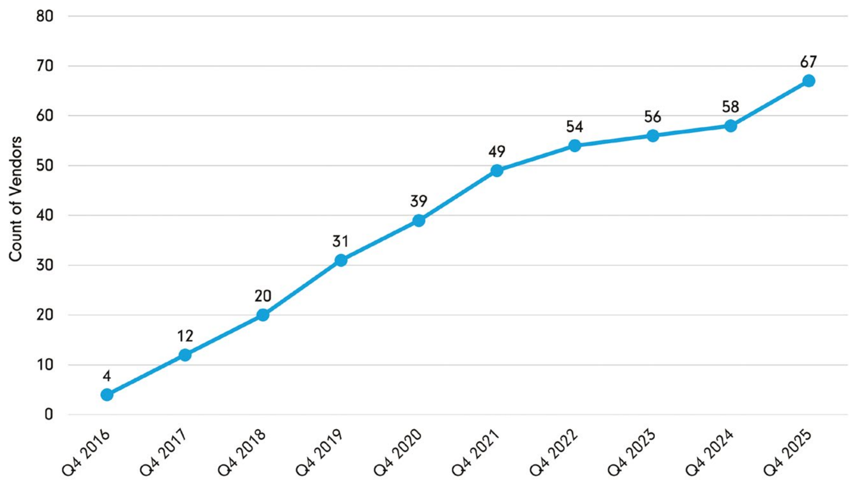
The feasibility of such automation may depend on IM differences remaining within agreed tolerance thresholds, which may present an opportunity for further standardization. Crucially, the ISDA SIMM's steady-state governance model provides the mechanism to safely pursue these enhancements.

9. Leverage the CRIF for risk representation in other contexts

A defining design principle of the ISDA SIMM is the separation of risk representation from calculation logic. By standardizing how portfolio and trade-level risk is described – independent of how margin is calculated – the ISDA SIMM established the Common Risk Interchange Format (CRIF) that supports reconciliation, benchmarking and validation across firms. This shared, extensible risk representation has enabled consistent implementation, facilitated third-party services, eased onboarding of new participants and supported key governance processes, including calibration and backtesting.

This design philosophy is directly reflected in the Common Domain Model (CDM). Just as the ISDA SIMM standardizes what risk looks like before defining how margin is calculated, the CDM standardizes what a trade or lifecycle event is before defining how it is processed. In both cases, the objective is to eliminate interpretative differences, reduce reconciliation breaks and enable deterministic processing across heterogeneous systems.

FIGURE 3: ISDA SIMM SERVICE PROVIDERS, 2017-2025



Source: ISDA

The same principles underpin ISDA's capital benchmarking and validation initiatives, which rely on consistent, comparable risk inputs to enable meaningful cross-firm analysis. The CRIF for standardized risk interchange could be useful in a wide variety of other contexts, including both industry initiatives and industry counterproposals to regulatory initiatives. These could include monitoring industry risk patterns, risk concentration analysis and profit-and-loss attribution.

10. Build on the ISDA SIMM ecosystem to accelerate future innovation

A decade of the ISDA SIMM has created more than just a model. It has established a mature ecosystem of market participants, service providers, data standards, governance processes and operational infrastructure. Significant industry investment has already been made in building and maintaining these capabilities, creating a foundation that extends well beyond the original objective of calculating IM.

As financial markets continue to evolve, this ecosystem could be leveraged to support new industry initiatives. Common standards such as the CRIF, established governance structures and a proven framework for industry collaboration provide valuable building blocks for addressing emerging challenges and developing new services. By building on existing foundations rather than creating entirely new solutions, the industry can reduce implementation costs, accelerate adoption and benefit from the trust and network effects already established through the ISDA SIMM.

The broader lesson is that successful industry standards can become platforms for future innovation. The ISDA SIMM demonstrates how a well-designed solution can generate lasting value by enabling new applications, services and forms of industry collaboration beyond the original mandate.

Foundation for the Future

The first decade of the ISDA SIMM demonstrates that robust financial market infrastructure is built not only on sound quantitative design, but on clear principles, pragmatic choices and credible governance, sustained by broad stakeholder engagement. What began as a focused response to regulatory reform has grown into a trusted global standard supporting hundreds of firms and hundreds of billions of dollars in IM.

As the derivatives market continues to evolve – particularly through advances in digital assets, automation and settlement infrastructure – the ISDA SIMM's established governance framework provides a robust mechanism for adapting prudently to change. The model's first decade suggests that its core strengths will remain relevant well into the future, enabling it to continue balancing operational practicality with global consistency in an increasingly complex financial system.

Marginal Gains

By pursuing greater harmonization and fine-tuning reporting and margining rules, the SEC and CFTC could significantly reduce operational burdens and improve the efficiency of the US derivatives market

In the early 2000s, some sports coaches became obsessed with the theory of marginal gains, which holds that small incremental improvements can create a significant competitive advantage. The same principle could be applied to the regulatory framework for derivatives markets in the US. The post-crisis reform agenda brought sweeping improvements in market stability and transparency, but implementation has also exposed areas of excessive burden and inefficiency that need to be addressed.

This won't amount to a complete revamp of the regulatory framework, but rather a focus on marginal gains to improve the experience of market participants and promote safe and efficient markets. While the US policy agenda is largely dominated by digital assets and innovation, the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC) have also committed to greater harmonization to realize the improvements that are needed.

"A lot of these issues will feel relatively small or extremely technical in nature. But they are definitely worth the effort to amend or improve, and we're keen to assist the regulatory agencies in this reform program. When you add the impact of all these imperfections together, they combine to create meaningful operational cost burdens and compliance headaches for market participants," says Adam Kezsbom, head of capital markets policy at Citi.

Reducing friction

For both the CFTC and the SEC, harmonization has emerged as a priority over the past year. Although the agencies were established to supervise different products and sectors, significant overlap has emerged over time, which has created added complexity for market participants – a challenge about which both have become increasingly vocal.

"For too long, the SEC and CFTC have operated in parallel lanes, too often in conflict with one another, leaving the American public to bear the costs of duplication, delay and uncertainty. That era is behind us," declared SEC chairman Paul Atkins at a joint roundtable in September 2025.

The momentum has accelerated in 2026, with a memorandum of understanding signed by the two agencies in March and a joint harmonization initiative established to support greater coordination across a range of key areas, including clearing, margining and regulatory reporting.

"From an industry perspective, enhanced regulatory alignment can improve transparency, streamline compliance processes and allow firms to focus resources on managing risk rather than navigating conflicting or duplicative requirements. While it may not attract the same attention as larger policy debates, continued progress towards greater cooperation could deliver meaningful benefits for both regulators and market participants over time," says Jenny Cosco, global head of government relations and regulatory strategy at the London Stock Exchange Group.

The harmonization agenda is likely to be a multi-year project, but the agencies have made a start by seeking industry input on certain key issues such as trade reporting. Under the Dodd-Frank Act, the CFTC oversees reporting for swaps, while the SEC is responsible for security-based swaps reporting, including single securities and narrow-based security indexes. But they diverge in certain key areas, including data format requirements and the way lifecycle events are reported.

This leaves market participants to shoulder the operational challenges and costs of running two separate reporting processes for similar products. Recognizing this, the SEC has published a series of no-action relief letters that enable market participants to rely, for the most part, on the CFTC rules to meet their security-based swaps reporting obligations until at least 2029.

But this is only a temporary solution. In June, the CFTC and SEC sought industry comment on ways to align their reporting frameworks while improving data transparency and reducing operational complexity. Adjustments to reporting formats and requirements might appear modest, but they collectively represent the kinds of marginal gains that could significantly reduce costs and improve efficiency for both market participants and regulators.

In its response to the consultation, ISDA argued that harmonization should be the guiding principle of any reporting reforms, urging the SEC to align with the CFTC's reporting framework wherever possible. The association also called for a rationalization of reporting requirements, recommending the removal of data elements that provide limited regulatory value, duplicate information available from other sources or add operational complexity without enhancing regulatory oversight.

"When these reporting rules were written 10 to 15 years ago, the answer to many questions was to collect more data. It's encouraging that regulators have begun to recognize that not all of the data collected today is useful and work with the industry to improve efficiency in this area," says Darcy Bradbury, managing director at the DE Shaw Group.

The harmonization agenda is also focused on the cross-border application of reporting rules. For example, the SEC specifies that security-based swap rules should be applied to any transaction between two non-US counterparties that is arranged, negotiated or executed using personnel located in the US, even if the risk of that transaction is held overseas. The CFTC ditched this concept in 2020, arguing it had no bearing on market stability and would disincentivize firms from operating in the US.

Market participants argue that this divergent approach creates confusion for non-US clients and introduces needless complexity for firms seeking to provide cross-border services. They would like to see a more consistent approach to substituted compliance across the two agencies.

"In many cases, the granular mapping of foreign and US rules simply isn't possible – foreign jurisdictions don't even recognize the distinction between swaps and security-based swaps in the way the US does. Attempting to do so merely adds complexity, cost and risk for no regulatory benefit," says Chris Young, head of US public policy at ISDA.

Margin

There are also important improvements to be made to margining processes to improve efficiency and risk sensitivity. One example is cross-margining – a vital industry practice that enables firms to more closely align their margin requirements with the risk of a portfolio of products, without having to make higher-than-necessary payments because offsets haven't been recognized.

Cross-margining programs already exist in the US and the CFTC and SEC have approved the extension of a joint program offered by the Fixed Income Clearing Corporation and CME Group to include clients as well as clearing members – a key step in enabling the efficient implementation of US Treasury clearing, which will begin for cash transactions at the end of this year.

But there is more to be done to eliminate the complexity and bureaucracy that has hindered the adoption of cross-margining in the past. Obtaining approval currently requires firms to navigate overlapping regulatory frameworks, inconsistent supervisory expectations and separate filings with the CFTC and SEC, often without a clear understanding of which standards apply or when a decision will be reached.

In its response to a consultation by the CFTC and SEC on how the approval of cross-margining programs could be improved, ISDA called for a joint review and approval framework, with transparent, principles-based criteria, a single application process and clearly defined timelines. ISDA also urged the CFTC and SEC to work with US prudential regulators – as well as their international counterparts – to ensure bank capital requirements do not prevent efficient cross-margining by recognizing risk offsets in a portfolio when calculating capital under the standardized approach for counterparty credit risk.

"Cross-margining programs are game-changing for our markets – they lead to lower liquidity demands, more efficient use of collateral and a closer alignment between margin requirements and actual risk. Yet adoption in the US has been slowed less by concerns about safety than by a maze of overlapping rules, duplicate reviews and administrative hurdles. The good news is that the CFTC and SEC have recognized the problem and are now looking at ways to streamline approvals and remove unnecessary barriers," says Scott O'Malia, chief executive of ISDA.

The CFTC has also taken steps to improve the flexibility of collateral management, which could contribute to greater resilience during periods of stress. Market participants have been looking to diversify their margin holdings to a wider range of high-quality liquid assets, rather than relying solely on cash and government securities. Money market funds (MMFs) would be a good option, with deep liquidity, low volatility and relatively small margin haircuts. But CFTC rules had previously prohibited the use of MMFs if the fund also engaged in securities lending, securities borrowing, repurchase agreements, reverse repurchase agreements or similar arrangements. In June, the CFTC removed this restriction, paving the way towards the use of MMFs as collateral, as long as similar changes are enacted by prudential regulators.

"We were encouraged by the CFTC's recent move on the MMF margin issue, and we'd welcome continued coordination with prudential regulators on this important topic. Enabling the use of these assets for initial and variation margin payments would significantly improve the efficiency and safety of the overall market, especially during times of heightened risk," says Bradbury.

"We were encouraged by the CFTC's recent move on the MMF margin issue, and we'd welcome continued coordination with prudential regulators on this important topic"

Darcy Bradbury, DE Shaw Group

This could also open the door to the use of tokenized MMFs as collateral – something ISDA has been focusing on as a way to reduce operational friction and liquidity risk in the derivatives market.

"The tokenization of MMFs is a highly compelling opportunity to improve the timeliness and efficiency of collateral management, which is why market participants have been focusing on the operational, legal and regulatory issues that must be addressed," says O'Malia. IQ

Standardize to Digitize

Smart contracts offer a highly effective way to automate key derivatives processes and eliminate manual intervention, but this cannot be achieved without the foundation of standardization provided by the Common Domain Model, writes ISDA's David Shone

Imagine a rates desk on a typical mid-week afternoon. A reset is due and an operations analyst is chasing a valuation before a credit support annex (CSA) threshold is breached. In another office, a member of the collateral team is keying yesterday's confirmed trades into a spreadsheet – a standard industry process still constrained by manual intervention and operational risk. Unfortunately, this is how a large part of the derivatives market still operates: carefully, repetitively and almost entirely dependent on people correctly applying the same well-understood rule thousands of times a day.

This repetitive daily grind has meant smart contracts have attracted growing attention as a way to bring about change – not because they promise anything magical, but because so much of that daily processing is precisely the kind of work that can be accurately coded using smart contracts.

At its simplest, a smart contract is a piece of code that automatically executes a pre-defined action once certain conditions are met, creating an automated version of a real-world contractual obligation. The concept has taken off since blockchains first appeared – in particular, since Ethereum arrived in 2015 – but the concept is older than that. US computer scientist Nick Szabo wrote about smart contracts in 1997, and coin-operated vending machines have long performed a very similar job: coins are inserted and evaluated by the machine, the required product is identified by its row and column, and the outcome – a snack deposited in the bottom of the machine together with any change – is achieved without human intervention. A smart contract is based on the same concept. Blockchains are not a prerequisite, but they've become a convenient way to run them.

SMART CONTRACTS IN BRIEF

- Smart contracts are programs that execute pre-defined actions when set criteria are met.
- A smart contract is not a legal contract – the ISDA Master Agreement still governs the full relationship.
- Resets, margin calls and close-out determinations are strong early candidates for automation via smart contracts because they are standardized and largely free of discretion.
- The Common Domain Model provides the common language needed for smart contracts to interoperate, rather than fragment firm by firm.

Derivatives use case

In the derivatives market, the use of smart contracts is easy to imagine. For example, a collateral call under a CSA typically requires a human to check a valuation, confirm a breach of the threshold and instruct a transfer. A smart contract could do the same job without the human – it would monitor the trigger and, once satisfied, move the collateral. The only thing that changes is how the obligation is executed. Crucially, smart contracts go beyond automation, which can already be achieved on an individual basis today. To create additional certainty, they are executed independently of the two parties in a way that gives them both full transparency, removing the need for reconciliation.

Multiply that single collateral call across a large derivatives book and the appeal becomes obvious: the same check, the same instruction, repeated many times a day across many counterparties, each one a small opportunity for delay, human error or a missed threshold. Because the task is so repetitive and rules-based, it lends itself well to automation. Underneath the label, the mechanics are fairly consistent, whatever the use case. The contract needs a reliable source of truth for whatever process it is carrying out – a valuation, a rate fixing or a settlement confirmation. This is typically obtained from an oracle – an external, trusted source of data that the contract cannot generate on its own. Once an agreed threshold is met, the logic is evaluated deterministically – there is no discretion and no second-guessing.

In practice, an oracle can be as straightforward as a market data feed for an interest rate fixing or a custodian confirming that a corporate action has settled. The smart contract trusts that feed absolutely, so the reliability of the oracle must be vetted thoroughly, as well as the logic of the smart contract itself.

If the condition is satisfied, execution and settlement typically happen together. That collapsing of decision and settlement into a single, immediate step is what gives smart contracts efficiency over the manual processes they replace, and also why getting the underlying code right matters so much.

Smart contracts are not without their limitations. Automating something that is poorly designed or controlled does not make the underlying problem go away. Instead, it scales it up – a small logic error, repeated across thousands of trades, very quickly becomes a large error.

On a public chain, the code is visible to anyone, but so are its bugs. Once a contract is deployed, it cannot always be changed, which is a very different risk profile to a legal agreement that can be amended by consent. Private or permissioned chains can mitigate some of this by restricting who can see the code and, in some designs, allowing controlled upgrades, but they trade away some of the transparency and resilience that make public chains attractive in the first place.

Despite its name, a smart contract is conceptually quite different from a legal contract. A smart contract is not a substitute for the ISDA Master Agreement, the schedule, the CSA or a confirmation. Those documents set out the full rights and obligations of the parties – representations, events of default, termination rights and close-out methodology – across a variety of scenarios, including those requiring judgment. In contrast, a smart contract automates some of the payments or deliveries that the legal agreement requires. A single derivatives transaction on a distributed ledger might involve several smart contracts. For example, there might be one for a reset, one for a margin call and one for a corporate action, with each automating one step of a lifecycle that the ISDA Master Agreement continues to govern in full.

CDM foundation

This is where the Common Domain Model (CDM) provides a platform for innovation. The CDM gives the market a shared language – a standard way of describing a trade, an event and an action, so two firms modeling the same occurrence (such as a reset or close out) use the same procedures to arrive at exactly the same answer. The CDM allows smart contracts to be built in a standard way.

To advance this idea and demonstrate the possibility, ISDA formed the CDM Smart Contract Taskforce, modeling a smart contract as a series of distinct steps starting with resets, because they are deterministic, parameter-driven and require no discretionary judgment. This work was delivered in CDM 7.0.

Eventually, the intention is to link the smart contracts back to the legal text – a version of the CDM in which a trade no longer references only the relevant ISDA Master Agreement and CSA by label and date but links to a digital representation of the pertinent clauses and their business outcomes. For example, a collateral substitution could draw on the specific clause for each counterparty, implemented by a smart contract underpinned by industry-agreed legal and technical standards, rather than bespoke code.

> "Smart contracts offer a practical route to automating specific, deterministic parts of the derivatives lifecycle"

Smart contracts offer a practical route to automating specific, deterministic parts of the derivatives lifecycle, but they should be seen as execution tools rather than replacements for the legal framework that governs the relationship between parties. Their value depends on a clear legal grounding, reliable data inputs, robust controls and a shared technical language.

This is where the CDM is so valuable: it provides the common structure needed to ensure automation is not fragmented, bespoke or disconnected from the underlying contractual terms. Used in the right way, smart contracts supported by the CDM can make post-trade processes faster, more consistent and more resilient, while maintaining the legal certainty provided by the ISDA documentation architecture.

None of this happens simply by writing more code. It depends on the market continuing to invest in standards like the CDM, on oracles that are trustworthy and on a realistic sense of where legal certainty genuinely exists today. Get those foundations right and smart contracts will no longer be a novelty running alongside the ISDA Master Agreement. Rather, they will become a faithful, interoperable expression of it, one deterministic step at a time. For a market that has spent decades building legal certainty clause by clause, this is a meaningful prize: automation that strengthens the framework it sits within, rather than working around it. IQ

David Shone is senior director, data and digital solutions, at ISDA

SMART CONTRACTS: FURTHER READING

ISDA has published extensive legal guidelines and articles on smart contracts, which are available online:

- Legal Guidelines for Smart Derivatives Contracts: Introduction – tinyurl.com/2m9y9442
- Legal Guidelines for Smart Derivatives Contracts: the ISDA Master Agreement – tinyurl.com/yx7umdp6
- Legal Guidelines for Smart Derivatives Contracts: Collateral - tinyurl.com/3bj3euhz
- Legal Guidelines for Smart Derivatives Contracts: Interest Rate Derivatives – tinyurl.com/yzks5wfe
- Legal Guidelines for Smart Derivatives Contracts: Equities – tinyurl.com/mwzv7mjb
- Legal Guidelines for Smart Derivatives Contracts: Foreign Exchange (FX) Derivatives – tinyurl.com/2tvxfjcr
- Legal Guidelines for Smart Derivatives Contracts: Credit Derivatives – tinyurl.com/jkfww3fp
- Private International Law Aspects of Derivatives Contracts Involving DLT – tinyurl.com/yermykt9
- Building Smart Contracts – tinyurl.com/m7ax6c7w

Reducing Burdens

As she nears the end of her term as chair of ESMA, ***Verena Ross*** *reflects on the EU's simplification and burden reduction agenda, the key regulatory priorities and the evolution of ESMA since she became its first executive director in 2011*

IQ: You're in your fifth year as chair of the European Securities and Markets Authority (ESMA) and coming to the end of your term at a time of increased fragmentation in the way major jurisdictions are approaching financial regulation. What impact has this had on your approach in leading ESMA and working with counterparts in other jurisdictions?

Verena Ross (VR): We are certainly living in very volatile and interesting times. The current geopolitical environment is clearly driving the strengthening of European capital markets, which is a key priority for ESMA. This is really about pushing for more effective European capital markets that can ultimately be attractive and support investors and companies in the EU – that is about better integration and less fragmentation. At the same time, we know that markets are global and we need to make sure we have a global approach. Wherever something goes wrong, it will percolate through the rest of the markets and market infrastructure, so we need to continue to work at a global level with our counterparts in the UK, the US and Asia, making sure we look at things from a global perspective. That has led to a lot of my focus being on representing European securities markets in global fora, while also strengthening and continuing to build our bilateral relationships with key regulators and supervisors globally.

IQ: One of the recommendations of the 2024 Draghi report on European competitiveness was that ESMA should transition from a body that coordinates national regulators to a common regulator for all European securities markets. What needs to happen to make that a reality?

VR: In a way, ESMA is already the common EU regulator, but this is about how we can build on that to become even more of a single European supervisor in certain areas. As well as the Draghi report, we also have the Savings and Investments Union, which is about how we can encourage savings and channel investment in capital markets, because we need to strengthen our capital markets to serve the European economy and its citizens. Part of that is also about reducing fragmentation and making sure the EU acts as a single capital market. The Market Integration and Supervision Package (MISP), which was published by the European Commission in December 2025, looks at how we can improve the trading, clearing and settlement environment, and also encourage digitization and innovation in European capital markets. This is about a lot of the supervision remaining at national level, rightly so, and looking at where it is most impactful and most important to think about harmonizing EU supervision, particularly for cross-border market infrastructure and crypto-asset players.

> "Simplification and burden reduction is a core priority for ESMA because we need to make sure the complexity and administrative burden that some regulation can produce is alleviated and we ultimately have rules that are streamlined, cost-efficient and easier to navigate"

IQ: MISP would give ESMA greater centralized supervisory powers for significant market infrastructures, such as trading venues, central counterparties and crypto-asset service providers. Why is this needed, and what will it mean for the entities being supervised and for ESMA itself?

VR: I think it will really improve the alignment between how markets function and how market players operate. The fact is that we have a single European market for goods and people, but what is missing is a single financial market that allows the borderless flow of capital. We have it in some ways, but we clearly need to strengthen it to break down the barriers that still hold some companies back from genuinely operating on an EU-wide level. So, the supervisory needs are just starting to reflect the reality of what is happening on the ground. The proposal is that ESMA would take on the direct supervision of key cross-border market infrastructures across trading, clearing and settlement and also strengthen convergence in those areas where supervision remains national to ensure greater consistency and common supervisory outcomes. That is a very natural evolution, creating greater clarity, reducing duplication and ensuring consistent outcomes in the way our supervision works in the European market.

IQ: The Draghi report estimated that a minimum annual investment of between €750 billion and €800 billion would be needed in key areas such as decarbonization, digitization, defense and competitiveness. Do you agree that derivatives will play an important role by improving access to funding, reducing borrowing costs and helping investors manage their risks, bringing greater stability and certainty?

VR: Certainly, derivatives markets are a very important part of capital markets. A lot of our capital markets would not function if there wasn't a well-functioning, transparent and orderly derivatives market. When

"We've ended up with a complex, often duplicative reporting regime, which has been subject to quite significant ongoing changes and led to costly continuing developments. We believe we can improve on that"

→ they think about capital markets, many people think first of all about equity and bond markets, but what is key is that we look beyond that because derivatives are an important aspect of supporting those markets, whether it's for hedging risks or managing exposures. Derivatives are an essential part of the efficient allocation of capital, and we need to ensure they function well and provide the transparency, robust infrastructure, including central clearing, and strong supervision to ensure they are trusted, stable and deliver for market players and investors.

IQ: In what ways is ESMA contributing to the simplification and burden reduction agenda that was spelled out in the Draghi report?

VR: Simplification and burden reduction is a core priority for ESMA because we need to make sure the complexity and administrative burden that some regulation can produce is alleviated and we ultimately have rules that are streamlined, cost-efficient and easier to navigate, whether that's for professional market players or for investors that want to engage in capital markets. We are very focused on simplifying regulatory and supervisory requirements where we can, making sure rules are more proportionate to the entity's size, nature and risk, and also improving the consistency and usability of all the work that we do. We decided very early on to focus our efforts on some of the key areas where we believe we can make the most substantive difference. We wanted to make our contribution to increase the EU's competitiveness, so we've looked at a number of flagship projects. Part of that is about regulatory reporting, whether that's transaction reporting or fund reporting, where we've looked deeply into what currently exists and how we can simplify it across the EU, either by breaking down some of the silos or by making sure we have a report-once principle. Another key focus is on making sure investors actually have the ability to look at disclosures in a simplified way, obtaining information that allows them to get the core background to investments so they can compare, reducing the complexity of some of the suitability and appropriateness assessments and simplifying some of the requirements on sustainability preferences. The final flagship project is making sure we have a common understanding of what risk-based supervision really means across the different supervisors operating in the EU. On top of all this, for any piece of legislation we are working on, or any mandate we get to formalize rules, we will make sure we look again to make them less complex.

IQ: ESMA recently published its final report on ways to simplify and reduce the burden of transaction reporting in the financial sector. This sets out a report-once approach that ESMA estimates could deliver annual net savings of up to €1 billion and a reduction in recurring costs of around 22%-24%. How can ESMA ensure this process results in material simplification and burden reduction?

VR: Because the Markets in Financial Instruments Regulation (MIFIR), the European Market Infrastructure Regulation (EMIR) and the Securities Financing Transactions Regulation (SFTR) have come at different times and been looked at in a siloed way, we've ended up with a complex, often duplicative reporting regime, which has been subject to quite significant ongoing changes and led to costly continuing developments. We believe we can improve on that and we are proposing a simplification of the regime with the report-once principle. At the same time, we should be clear that transaction reporting has a critical role to play in terms of market transparency, monitoring risks and detecting market abuse – these are essential reports for public authorities at large. We are also very clear that we need to do this in two phases – reducing some of the burdens quickly in the short term and then taking a more structural long-term reform approach. We are working now to make sure we create a single integrated transaction reporting framework across MIFIR, EMIR and SFTR, and we are also trying to implement some immediate improvements.

IQ: The digital assets market is evolving rapidly in the US and regulators are working to develop a regulatory framework. How does that compare with the approach in the EU?

VR: We have been working quite intensively over the past few years to create a common European framework, particularly in the crypto-asset space with the Markets in Crypto-Assets Regulation (MICA). We are very pleased to see a clear framework that allows for consistent approaches across the EU, rather than what we had before with a number of different national regimes. That is helping to deliver consistent investor protection and reduce the arbitrage that was previously possible within different parts of the market. We are working closely with the national competent authorities to make sure MICA is applied consistently. We want to ensure that, in this market, which is inherently cross-border, we have a single European supervisory approach. The key aim is to have a crypto market that is trusted by investors, is stable and creates a competitive and level playing field in the EU. One of the challenges is the interoperability between these different players and the interoperability between the crypto tokenized space and the traditional financial market space. I think that's where the real challenge lies – how will that develop and what are the turning points that will allow a broad-scale tokenized market to emerge that is embedded in the same rights and legal principles as we have in traditional financial markets?

IQ: Against the backdrop of an increasingly complex global political environment, how do you see ESMA's role in sustainable finance evolving?

VR: Sustainable finance remains a political priority in the EU. It's also something that ESMA has focused on over the past few years, with the aim of ensuring investors receive reliable information, that market integrity is supported and ultimately that investors can make choices about how much they want to support sustainable finance and the transition to a more sustainable economy. ESMA has had an expansion of our supervisory mandates with environmental, social and governance ratings providers coming into our remit this year, as well as EU green bond verifiers. We see investment in these types of instruments still being quite attractive for many investors. At the same time, we know that some of the sustainable finance regulatory framework has been quite complex and has often been developed at high speed and not necessarily with the best phasing, so this is being reviewed. ESMA is supporting that process, making sure the framework is clear, consistent and as simple as possible, while providing the right information to investors. It will also be about continuing to build the shared supervisory culture and consistent outcomes, like we do in all of our convergence activity. Ultimately, we want to see a framework that is trusted, workable and helps to support the green transition, while remaining proportionate in its approach. This is another area where deep and integrated EU capital markets will make a real difference.

IQ: You will step down from ESMA at the end of October, having been with the agency since it was established in 2011 and serving as its first executive director. What have been the highlights and how has it compared with previous roles?

VR: It certainly has been a fascinating, eventful journey, with many fantastic achievements. ESMA started out after the global financial crisis and in the middle of the EU sovereign debt crisis, so a lot of it was about fixing some of the fundamental issues in our regulatory framework. We were initially very much a rule-maker trying to harmonize some of the detailed EU-level regulation. And then we focused a lot on implementation, on making sure we had a convergent and common approach in how we implement and supervise. We also took on some supervisory mandates at the very beginning, but that has clearly matured and we have grown into a respected risk-based supervisor in the limited areas where we do have that power.

I think we've built a strong reputation and we provide the common European supervisory approach to strengthen EU capital markets. At this point in time, I believe we can be trusted to take on additional responsibilities as a direct supervisor. We've been able to take on other mandates and manage through quite difficult periods, thanks to a great team that comes from all corners of Europe and good work with our board members from the national competent authorities. What has been really special is that European spirit of building something that is genuinely cross-border, breaking through some of those national perspectives and being stronger together. We have managed to build a strong European organization that supports the unique European capital market. IQ

This is a shortened version of a recent interview with Verena Ross on *The Swap* podcast. Listen to the full episode here: tinyurl.com/yc2u5ze4

"Certainly, derivatives markets are a very important part of capital markets. A lot of our capital markets would not function if there wasn't a well-functioning, transparent and orderly derivatives market"

A Safer Market

*More than 40 years on from the development of the first standard derivatives documentation in the1980s, **Thomas Jasper**, ISDA's first co-chair, has written a memoir in which he reflects on the extraordinary growth of the derivatives market*

As a trader and risk manager since the early 1980s, I've been fortunate to participate in several significant changes in the derivatives market, starting with the creation of ISDA in 1985 and the development of the Code of Standard Wording, Assumptions and Provisions for Swaps. Having served as ISDA's first co-chair, I am very pleased that it remains a driving force in derivatives markets more than 40 years later.

Writing my memoir, *Wall Street Maverick: Musings on a Career of Innovation, Derivatives, Credit, and Risk*, has given me the opportunity to reflect on those early days of my career and the development of the derivatives market we know today. Back in the 1980s, there was very little liquidity in interest rate swaps (IRS) and many bank participants were resistant to trading this new product. But there was a core of IRS dealers that felt trading was the future of the market and participation needed to be broadened.

So began a period of innovation in which IRS dealers like Salomon Brothers, where I worked, began to develop the foundations for trading in the derivatives market. There was a significant focus on how to value the cashflows associated with IRS and how to hedge those changes in value. Other steps included defining what it meant to intermediate the two cashflows and how to assess and manage counterparty risk. By the late 1980s, IRS were being actively traded, with dealers offering market participants good liquidity at relatively tight bid-offer spreads. IRS were being quoted on a screen for the first time and dealers were willing to go long and short.

Later in my career, in the early 2000s, I witnessed significant growth and innovation in the credit default swap (CDS) market across a broad spectrum of credit risk. It was a very exciting time as CDS were being widely used to manage and trade credit risk. In many respects, that supplanted the bond market as the go-to place to assess credit quality and liquidity. During the global financial crisis in 2008, it became clear there were some bad actors in the market – in my view, CDS and the leverage embedded in some of the more structured trades contributed to the crisis. ISDA played an important role in addressing a number of complex issues that arose during the financial crisis. For example, I served on the first Credit Derivatives Determinations Committee, which, among other things, determined whether a credit event had occurred.

> "The modern derivatives market is a vital component of the global financial system, and much safer than it used to be"

Today, I see a much larger and more liquid derivatives market than I would ever have dreamt of in the 1980s, with a wide spectrum of products traded around the world. The modern derivatives market is a vital component of the global financial system, and much safer than it used to be. In the early days, counterparty risk was not well understood and many institutions equated swap risk with loan risk. ISDA developed the first close-out methodology to be used in the event of a counterparty default, but there was no margining back then, and the technology to assess daily mark-to-market valuation changes was still in its infancy. Regulators had only a very basic understanding of how IRS worked, let alone being able to assess systemic risks.

All that has changed. Credit support annexes are now standard practice for the mitigation of counterparty credit risk and more than 80% of the interest rate derivatives market is now centrally cleared. There is also much broader regulatory oversight of the derivatives market. All this has contributed to a much safer and more resilient market.

That doesn't mean there are no remaining vulnerabilities, of course. As the derivatives market continues to grow and innovate, it is vital that the products are always well understood and properly documented.

I am sure the derivatives market has an exciting future ahead. Electronic trading already accounts for more than 60% of the derivatives market, providing greater transparency, efficiency and liquidity than in the early days. Artificial intelligence (AI) will also play a significant and expanding role in the trading and management of derivatives portfolios. The obvious starting point is derivatives documentation, where AI can assume the role of legal associates charged with documenting transactions. That first step will be followed by the use of AI to create the algorithmic strategies to trade and manage risk. It will make the market even more efficient, but there will also be challenges that must be managed and I don't think it will be a substitute for smart traders and portfolio managers.

As the derivatives market continues to grow in volume, I believe this is the sign of a healthy market that has never stopped innovating and attracting new participants. It's a far cry from the early days of IRS trading in the 1980s, but the focus on managing and reducing risk has never wavered. IQ

Wall Street Maverick: Musings on a Career of Innovation, Derivatives, Credit, and Risk by Thomas Jasper will be published by Amplify Publishing on September 29

MISSION STATEMENT

ISDA fosters safe and efficient derivatives markets to facilitate effective risk management for all users of derivative products

STRATEGY STATEMENT

ISDA achieves its mission by representing all market participants globally, promoting high standards of commercial conduct that enhance market integrity, and leading industry action on derivatives issues.

THE PREEMINENT VOICE OF THE GLOBAL DERIVATIVES MARKETPLACE

Representing the industry through public policy engagement, education and communication

AN ADVOCATE FOR EFFECTIVE RISK AND CAPITAL MANAGEMENT

Enhancing counterparty and market risk practices and ensuring a prudent and consistent regulatory capital and margin framework

THE SOURCE FOR GLOBAL INDUSTRY STANDARDS IN DOCUMENTATION

Developing standardized documentation globally to promote legal certainty and maximize risk reduction

A STRONG PROPONENT FOR A SAFE, EFFICIENT MARKET INFRASTRUCTURE FOR DERIVATIVES TRADING, CLEARING AND REPORTING

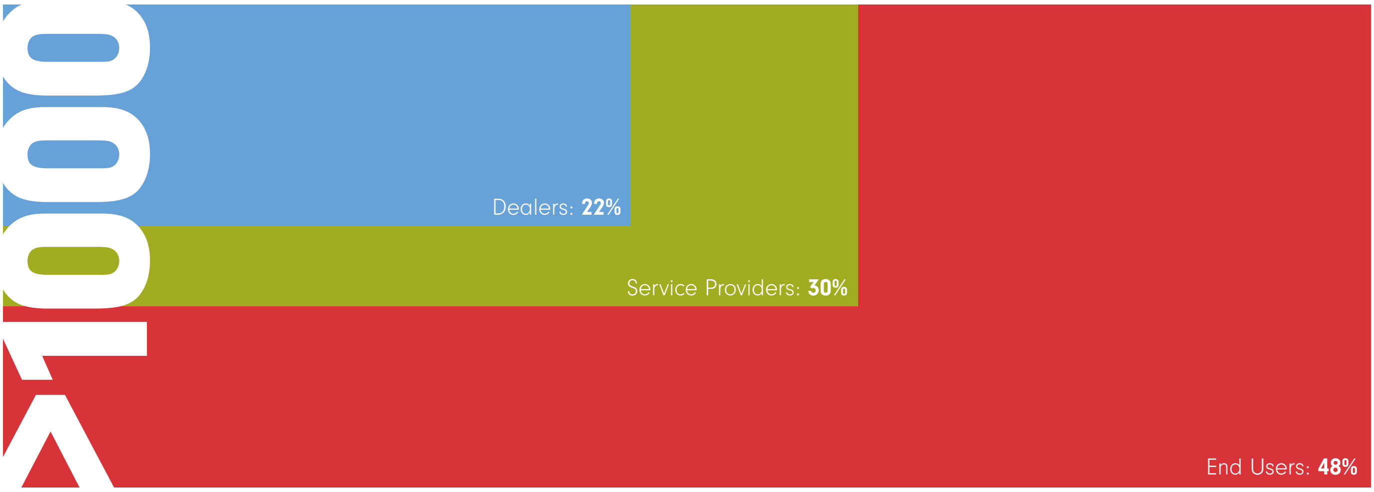
Advancing practices related to trading, clearing, reporting and processing of transactions in order to enhance the safety, liquidity and transparency of global derivatives markets

www.isda.org

MEMBERSHIP INFORMATION

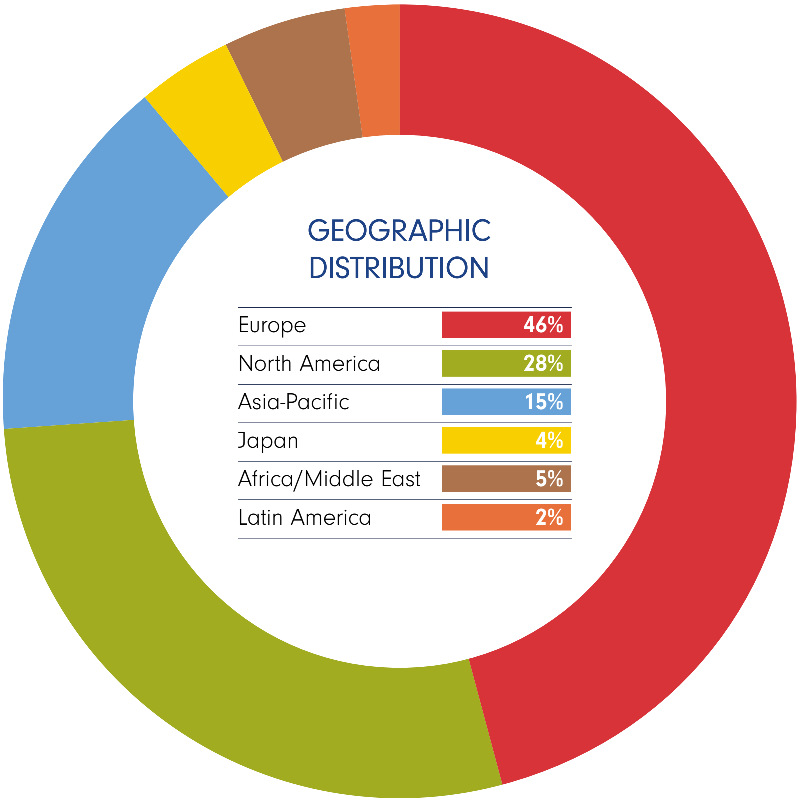
ISDA has over 1,000 members from 79 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers.

MEMBERSHIP BREAKDOWN



TYPES OF MEMBERS

Banks	32%
Law Firms	21%
Asset Managers	9%
Government Entities	13%
Energy/Commodities Firms	7%
Diversified Financials	6%
Technology/Solutions Providers	4%
Other	8%



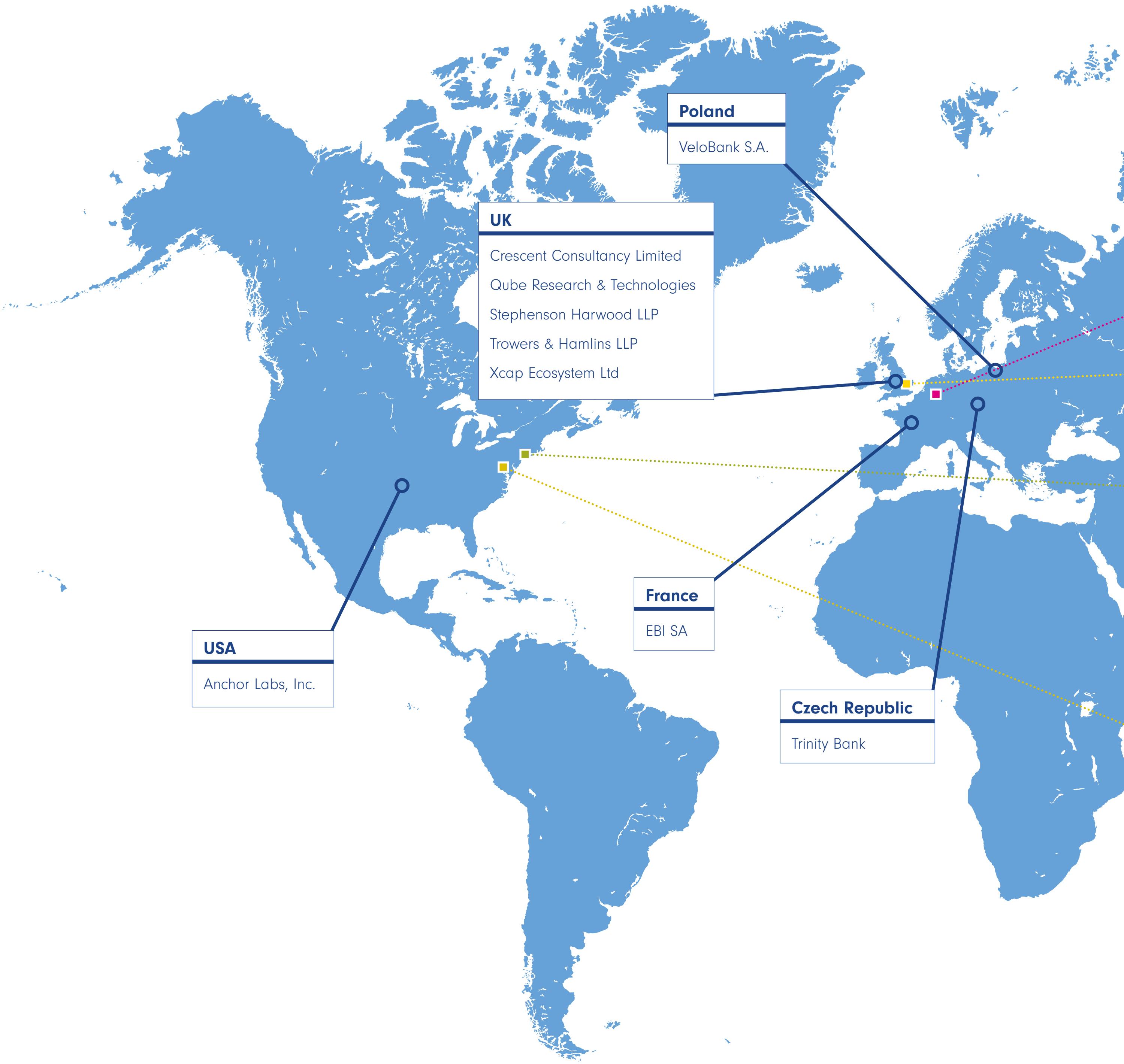
GEOGRAPHIC DISTRIBUTION

Europe	46%
North America	28%
Asia-Pacific	15%
Japan	4%
Africa/Middle East	5%
Latin America	2%

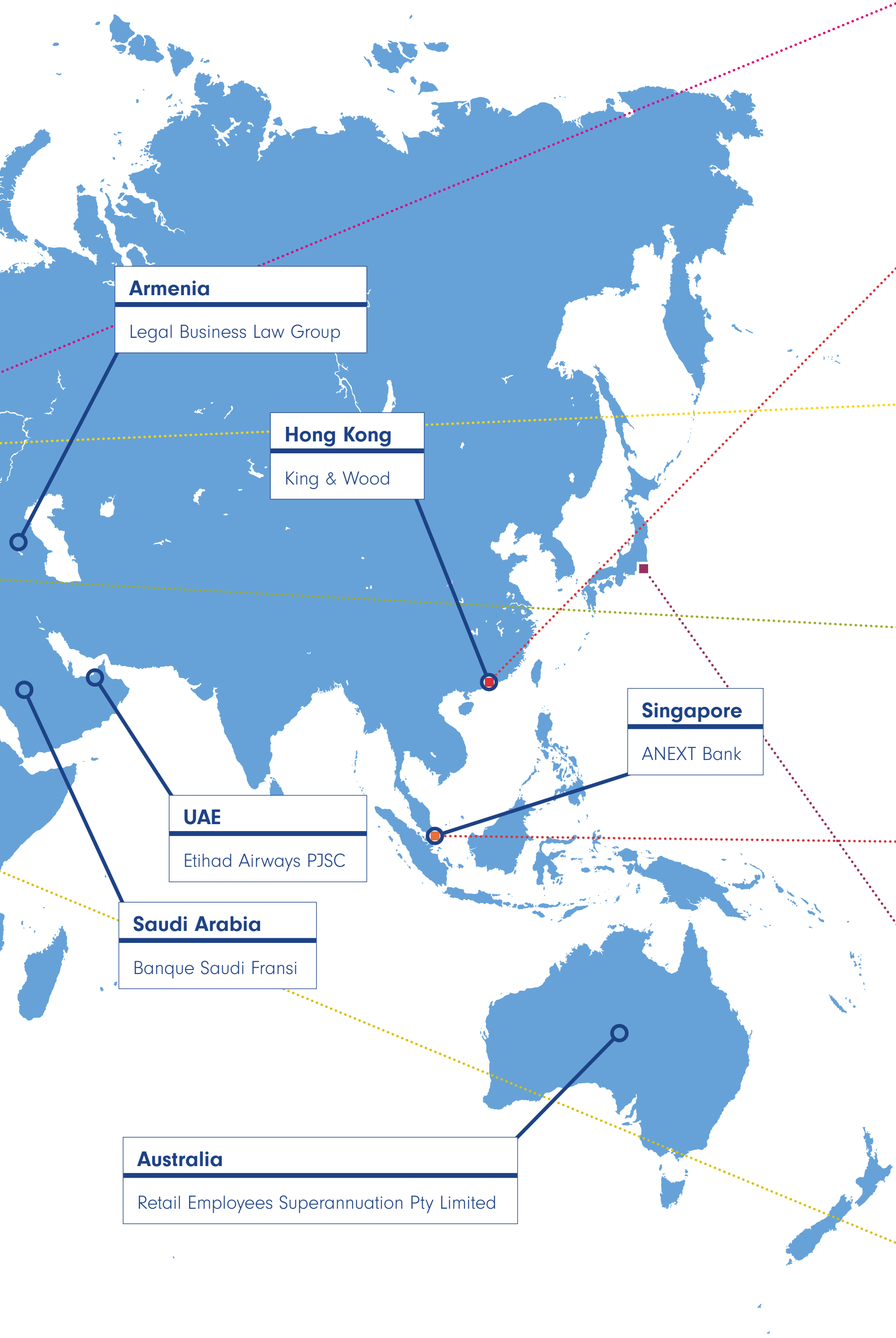
Additional information regarding ISDA's member types and benefits, as well as a complete ISDA membership list, is available on the ISDA Membership Portal: https://membership.isda.org/

NEW ISDA MEMBERS

A big welcome to all new members that have recently joined ISDA. We look forward to working with you in the future



For additional information on joining ISDA, please visit the ISDA Membership



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"A lot of our capital markets would not function if there wasn't a well-functioning, transparent and orderly derivatives market"

Verena Ross, European Securities and Markets Authority