ISDA Safe, Efficient Markets

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Opening remarks
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Hello everyone, and welcome to the ISDA European Public Policy virtual conference. Thanks for joining us today and thank you to all our speakers.

We've now entered the final month of the Brexit transition period, which means that in just over four weeks' time, a new chapter will begin for both the European Union (EU) and the UK. The road to Brexit since the 2016 referendum has been long and complex, but ISDA has consistently made the case for the continuity of cross-border derivatives trading. That remains our objective in this final phase of the UK's withdrawal.

By far the best way of ensuring continuity of cross-border trading is through equivalence determinations. Equivalence enables mutual recognition of the regulatory regimes in two jurisdictions. With equivalence in place, both sides benefit, and the cross-border market can flourish.

We are very grateful to the European Commission for its decision in September to adopt a time-limited equivalence decision for central counterparties (CCPs) until mid-2022. Last month, the UK announced a series of unilateral equivalence decisions designed to ensure continuity for UK firms trading with EU entities, which also included equivalence for EU CCPs. The combined effect should avoid any disruption in clearing when the Brexit transition period ends.

Despite this progress, we remain very concerned about the lack of equivalence for trading venues. On November 25, the European Securities and Markets Authority (ESMA) announced that the EU derivatives trading obligation will continue to apply without any changes after the end of the Brexit transition period.

With no agreement in place, UK and EU firms will be unable to use trading venues in the other jurisdiction for contracts within scope of the derivatives trading obligation. In fact, their only option, if they want to trade with each other, might be to use US swap execution facilities, which are recognized by both jurisdictions. This would pose certain operational and practical challenges. EU entities trading derivatives through a UK branch with a UK counterparty also face difficulties as they would be in scope of both the EU and UK derivatives trading obligations.

In September, ISDA published a paper that highlighted some possible partial alternatives to equivalence, such as a change in the application of the derivatives trading obligation to mitigate the impact on business conducted through overseas branches. But the alternatives would be inferior to equivalence as a solution to the current impasse. Equivalence remains by far the most effective option to avoid fragmentation of liquidity and increased operational costs, particularly as the trading venue rules in the EU and UK are virtually identical. Both sides should work towards trading venue equivalence as a priority.

The end of the Brexit transition period comes against a backdrop of a very busy agenda in Europe. We'll hear later on about the review of both the second Markets in Financial Instruments Directive framework and the EU Benchmarks Regulation (BMR), but I'd like to offer a couple of observations as we reach a critical phase in the BMR review.

ISDA strongly supports the wholesale review of the BMR as a means of achieving a more robust, proportionate and effective regulatory regime for benchmarks used in the EU. Two particularly important issues should be addressed.

First, the third-country regime remains a source of concern. Equivalence, which was intended to be the main route for qualifying third-country benchmarks for use in the EU, covers only a handful of benchmarks. The other two qualification routes – endorsement and recognition – are difficult, costly and unattractive. This means very few third-country benchmarks have qualified to date.

Allowing the current transition period for third-country benchmarks to expire at the end of 2021 without wholesale reform would adversely impact the ability of European companies to compete in the global market. It could also restrict pension funds, insurance companies, banks and investors that rely on products referencing third-country benchmarks for hedging and investment. That is why ISDA and 13 other trade associations last month published a joint paper making the case to extend the transition period to the end of 2025.

Earlier this week, we understand the European Parliament and council agreed to extend the transition period until the end of 2023. We are grateful for this additional time, and a more comprehensive review of the BMR must now address the deficiencies of the third-country regime in a practical and proportionate way. This should be completed in good time before the transition period expires.

Second, it is critical that parties complying with IBOR reforms and the EU requirement to incorporate fallbacks across all derivatives asset classes do not find those pre-European Market Infrastructure Regulation (EMIR) contracts subject to EMIR clearing and margining requirements. Recent amendments to EMIR addressed this issue for interest rate derivatives contracts, but uncertainty remains over which methods of compliance with IBOR reform are covered by this relief and whether other asset classes are covered by the relief relating to fallbacks.

We understand there has also been agreement at a political level to address this issue. ISDA welcomes this development as it will avoid a situation in which firms are discouraged from compliance with benchmark reforms. This clarity should help to strengthen the contractual robustness of their contracts.

I have talked in these remarks about our short-term priorities as we move through the end of the Brexit transition period and finalize the BMR Review. But there is, of course, a long-term outlook as well. You can count on ISDA to ensure market participants have the necessary tools, solutions and documentation to continue to operate efficiently in the post-Brexit world. We will also continue to help our members comply with regulatory requirements in the most cost-effective way possible.

With such a full policy agenda, we are grateful to regulators for their ongoing cooperation and support. Two recent developments have been particularly welcome.

First, ESMA's report on post-trade risk reduction on November 10 concluded that a limited and qualified exemption from the clearing obligation for compression or rebalancing trades would support the reduction of both risk and complexity. Second, on November 23, the European Supervisory Authorities published draft regulatory technical standards relating to the clearing obligation and margin requirements. These standards grant and extend critical relief for Brexit-related novations, equity options and cross-border intragroup transactions. This relief will be helpful to firms in many ways, including making it easier to manage risk centrally, allocate liquidity and compete with firms in other jurisdictions.

We are delighted to have several European regulators with us today, and I'm looking forward to hearing their perspective on the priorities and challenges ahead. First, let me introduce Fabrizio Planta, head of markets and data reporting department at ESMA.