



## Derivatives Update

November 18, 2011

### *European Parliament approves regulation banning naked sovereign CDS*

The European Parliament approved a regulation to limit short selling and certain trading of credit default swaps (CDS), in order to reduce speculation on sovereign default.

The regulation will ban naked sovereign CDS but allow Member States to temporarily suspend the ban, for up to twelve months with the potential for extending the suspension for another six months, if liquidity in their sovereign debt comes under pressure. The criteria for suspension of the ban and the definition of what constitutes a naked CDS position will be determined at a later stage by the European Securities and Markets Authority (ESMA).

In terms of next steps, the European Council also needs to formally approve this version of the regulation, which is expected in the coming weeks. The regulation applies from November 2012.

### *House Financial Services Committee approves four swaps-related bills*

On November 15, the US House Financial Services subcommittee on capital markets approved four swaps-related bills which refine the Dodd-Frank Act's definition of a swap execution facility (SEF), exempt inter-affiliate swaps from certain Dodd-Frank requirements, ensure that pension plans are able to use swaps for hedging purposes and repeal the swaps push-out provision. The bills would next need to be adopted by the House and then will move to the Senate, where there is little chance they gain approval.

The bills are summarized in greater detail below:

- **SEF definition:** The approved measure mandates the Commodity Futures Trading Commission (CFTC) and Securities and Exchange Commission (SEC) to allow greater flexibility in the types of trading methods permissible on SEFs. The measure places restrictions on the requirements that the CFTC and SEC can impose on SEFs and their participants, including preventing the regulators from (i) requiring participants to request quotes from a minimum number of sources; (ii) requiring SEFs to display or delay quotes for a specific period of time; (iii) requiring trading systems to interact on the same SEF; and (iv) limiting participants from using means of interstate commerce to execute transactions.



- **Inter-affiliate swaps:** The approved measure would exempt transactions between parties under common control (inter-affiliate swaps) from the definition of “swap” and therefore exempt these transactions from the clearing, reporting and margin requirements under Dodd-Frank.
- **Pension plans:** The approved measure would ensure that eligible pension plans are able to conduct swap transactions to mitigate their risk.
- **Swaps push-out:** The approved measure would repeal provision 716 of the Dodd-Frank Act which requires banks that have access to deposit insurance from the Federal Reserve’s discount window to move some of their swap activities to separately capitalized, non-bank affiliates.

### *BIS releases report on CCPs in OTC derivatives markets*

On November 17, the Bank for International Settlements Committee on the Global Financial System (CGFS) released a report entitled ***The Macroeconomic Implications of Alternative Configurations for Access to Central Counterparties in OTC Derivatives Markets.***

The report examines the various alternative access arrangements that are currently under consideration for the central clearing of OTC derivatives trades, including the establishment of domestic central counterparties (CCPs) and the possible benefits of establishing links between them. The report notes that the conditions under which market participants obtain access to central clearing could have important implications for financial stability and efficiency. The report concludes that:

- Expanding direct access to CCPs may reduce concentration risk in large global dealers. As direct access is broadened, it is essential that CCPs’ risk management procedures be adapted appropriately to ensure their continued effectiveness;
- Both large global and smaller regional CCPs will play a role in meeting G20 commitments. In both cases, adopting international standards will be essential to avoid regulatory arbitrage and promote effective cross-border monitoring of infrastructure and participants; and
- CCPs and authorities should consider enhancements to strengthen the safety and efficiency of indirect clearing that comply with international standards. Effective segregation, as well as portability of positions and collateral belonging to a direct clearer’s clients, are crucial to realize the benefits of systemic risk reduction.

The full report can be found at: <http://www.bis.org/publ/cgfs46.htm>

## **Forward calendar**

### **EMEA**

- **Q4 2011 (November 28, 2011):** Target date for political agreement on EMIR legislation
- **Spring 2012:** Target date for adoption of EMIR legislation
- **Mid 2012:** European Commission and ESMA to publish finalized, detailed EMIR rules
- **End 2012:** Target date for EMIR rules to be implemented in the EU

### **Americas**

- **December 5, 2011:** CFTC open meeting to discuss Dodd-Frank rulemakings



- The expected timing of CFTC/SEC Dodd-Frank rulemakings is summarized below:

<b>CFTC: Remainder of 2011</b>	<b>First Quarter 2012</b>
<ul style="list-style-type: none"> <li>Clearinghouse Rules</li> <li>Data Recordkeeping and Reporting</li> </ul>	<ul style="list-style-type: none"> <li>Capital and Margin</li> <li>Client Clearing Documentation and Risk Management</li> </ul>
<ul style="list-style-type: none"> <li>End-User Exception</li> <li>Entity Definitions/Registration</li> <li>External Business Conduct</li> <li>Internal Business Conduct (Duties, Recordkeeping and Chief Compliance Officers)</li> </ul>	<ul style="list-style-type: none"> <li>Conforming Rules</li> <li>Disruptive Trading Practices</li> <li>Governance and Conflict of Interest</li> <li>Internal Business Conduct (Documentation)</li> </ul>
<ul style="list-style-type: none"> <li>Position Limits</li> <li>Product Definitions/Commodity Options</li> <li>Real-Time Reporting</li> <li>Segregation for Cleared Swaps</li> <li>Trading - Designated Contract Markets and Foreign Boards of Trade</li> </ul>	<ul style="list-style-type: none"> <li>Investment of Customer Funds</li> <li>Swap Execution Facilities</li> <li>Segregation for Uncleared Swaps</li> <li>Straight-Through Trade Processing</li> </ul>
<b>SEC: Remainder of 2011</b>	<b>First Half 2012</b>
<ul style="list-style-type: none"> <li>Registration and regulation of SBSs and SBMSPs (proposed)</li> <li>Final Reg. SBSR – Reporting and Dissemination of SBS Information</li> <li>Final Rule on SBSDR Registration, Duties, and Core Principles</li> </ul>	<ul style="list-style-type: none"> <li>Final SEC Rule on Anti-fraud in connection with SBSs</li> <li>Final SEC Rule on Registration and Regulation of SBS SEFs</li> <li>Final SEC Rule on Ownership Limitations and Governance Requirements for SBS Clearing Agencies, SBS SEFs, and National Securities Exchanges wrt SBSs Under Regulation MC</li> </ul>
<ul style="list-style-type: none"> <li>Final SEC Rule on End-User Exception to Mandatory Clearing of SBSs</li> <li>Final SEC Rule on Process for Review of SBSs for Mandatory Clearing and Notice Filing Requirements for Clearing Agencies; and technical amendments to Rule 19b-4</li> </ul>	<ul style="list-style-type: none"> <li>Final SEC Rule regarding the registration and regulation of SBSs and MSBSPs</li> </ul>
<ul style="list-style-type: none"> <li>Final CFTC/SEC Rule on Definition of "Swap," "SBS," and "SBS Agreement"; Mixed Swaps; SBS Agreement Recordkeeping</li> </ul>	
<ul style="list-style-type: none"> <li>Final CFTC/SEC Rule on Definition of "SD," "SBSD," "MSP," "MSBSP" and "ECP"</li> </ul>	

### AsiaPac

- Hong Kong, November 30, 2011:** HKMA/SFC deadline for consultation on proposed regulatory regime for the OTC derivatives market
- Singapore, Q4 2011:** MAS consultation on G20 OTC derivatives reforms
- Australia, Q2 2012:** Consultation on clearing and settlement infrastructure oversight



- **Japan, Q3 2012:** New CCP to begin clearing interest rate swaps
- **Hong Kong, Q3 2012:** HKMA trade repository and HKEx CCP begin

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