

Derivatives, Legislative and Regulatory Weekly Update (April 8, 2024)

Client Alert | April 8, 2024

From the Derivatives Practice Group: ISDA submitted responses to proposals from various bodies this week, both domestically and abroad.

New Developments

- **CFTC's Energy and Environmental Markets Advisory Committee to Meet.** The CFTC's Energy and Environmental Markets Advisory (EEMAC) will hold a public meeting from 9:00 a.m. to 12:00 p.m. (CDT) on Wednesday, April 10 at the University of Missouri – Kansas City in Kansas City, Missouri. At this meeting, the EEMAC will continue its discussion on the federal prudential financial regulators' proposed rules implementing Basel III and the implications for and impact on the derivatives market. There will also be presentations and discussions on the state of crude oil markets and the future of power markets. Finally, the two EEMAC subcommittees will offer updates on their continued work related to traditional energy infrastructure and metals markets.
- **CFTC's Agricultural Advisory Committee to Meet.** The CFTC's Agricultural Advisory Committee (AAC) will hold a public meeting on April 11 from 9:30 a.m. to 11:00 a.m. (CDT) at the Sheraton Overland Park Hotel in Overland Park, Kansas. At this meeting, the AAC will discuss topics related to the agricultural economy and recent developments in the agricultural derivatives markets.
- **SEC Adopts Reforms Relating to Investment Advisers Operating Exclusively Through the Internet.** On March 27, the SEC adopted amendments to the rule permitting certain internet investment advisers to register with the Commission (the "internet adviser exemption"). The amendments will require an investment adviser relying on the internet adviser exemption to have at all times an operational interactive website through which the adviser provides digital investment advisory services on an ongoing basis to more than one client. The amendments will also eliminate the current rule's de minimis exception by requiring an internet investment adviser to provide advice to all of its clients exclusively through an operational interactive website and to make certain corresponding changes to Form ADV.
- **CFTC's Market Risk Advisory Committee to Meet.** The CFTC's Market Risk Advisory Committee (MRAC) will meet on April 9 at 9:30 am ET. The MRAC will introduce recommendations, reports and presentations on current topics and developments, including an approach to manage the resilience, recovery or wind down of central counterparties, the implications of concentration risk in intermediation, the U.S. treasury cash-futures basis trade and risk-management considerations, a work plan for the integration of artificial intelligence in the markets; possible recommendations regarding efforts to manage climate-related market risks; and updates on the work of several workstreams on block implementation rules, post-trade risk reduction services, and margin transparency, margin procyclicality and margin calls.

New Developments Outside the U.S.

- **UK's Accelerated Settlement Taskforce Publishes Report on the Path to T+1.**

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On March 28, the UK's Accelerated Settlement Taskforce published its [report on the path to a T+1 settlement cycle](#). The report finds there is a clear consensus on the need for the UK to move to a T+1 settlement cycle and this shift will require substantial investment in greater automation and standardization. In addition, the report emphasizes a need for ongoing engagement with stakeholders during the transition period and the opportunity to learn from the U.S. move to T+1 in May 2024. The report recommends the immediate creation of a technical group to identify the challenges of transition and formulate solutions and suggests a two-step transition to T+1 before the end of 2027, with the exact date to be determined by the technical group. [NEW]

- **ESMA Clarifies Application of Certain MIFIR Provisions, Including Volume Cap.** On March 27, the European Securities and Markets Authority (ESMA) published a [statement](#), including practical guidance supporting the transition and the consistent application of the revised Markets in Financial Instruments Regulation (MiFIR). The statement covers guidance on equity transparency and non-equity transparency; the systematic internaliser (SIs) regime; designated publishing entities (DPEs); and reporting. Regarding the volume cap, following the publication by the European Commission, ESMA confirmed that DVC data will continue to be published, with the next publication scheduled for early April.
- **ESMA Provides Market Participants with Guidance on the Clearing Obligation for Trading with 3rd Country Pension Schemes.** On March 27, ESMA issued a [public statement](#) on deprioritizing supervisory actions linked to the clearing obligation for third-country pension scheme arrangements (TC PSA), pending the finalization of the review of EMIR. ESMA expects National Competent Authorities (NCAs) not to prioritize supervisory actions in relation to the clearing obligation for derivative transactions conducted with TC PSAs exempted from the clearing obligation under their third-country's national law. Additionally, ESMA recommends that NCAs apply their risk-based supervisory powers in their day-to-day enforcement of applicable legislation in this area in a proportionate manner. The Council and the European Parliament reached a provisional agreement on February 7. The political agreement on the EMIR 3 text provides for an exemption regime from the EMIR clearing obligation when the TC PSA is exempted from the clearing obligation under that third country's national law.
- **ESMA Finalizes First Rules on Crypto-Asset Service Providers.** On March 25, ESMA published the [first Final Report](#) under the Markets in Crypto-Assets Regulation (MiCA). ESMA stated that the report, which aims to foster clarity and predictability, promote fair competition between crypto-asset service providers (CASPs) and a safer environment for investors across the Union, includes proposals on: (1) information required for the authorization of CASPs; (2) the information required where financial entities notify their intent to provide crypto-asset services; (3) information required for the assessment of intended acquisition of a qualifying holding in a CASP, and (4) how CASPs should address complaints.
- **ESMA Launches the Third Consultation Under MiCA.** On March 25, ESMA published its [third consultation package](#) under the MiCA. In the consultation package, ESMA is seeking input on four sets of proposed rules and guidelines, covering: (1) detection and reporting of suspected market abuse in crypto-assets; (2) policies and procedures, including the rights of clients, for crypto-asset transfer services; (3) suitability requirements for certain crypto-asset services and format of the periodic statement for portfolio management; and (4) ICT operational resilience for certain entities under MiCA.
- **SGX Issues Consultation on Revised Limit on Clearing Members' Liability for Multiple Defaults.** On March 22, Singapore Exchange (SGX) issued a [consultation paper](#) proposing to refine the existing cap on a clearing member's liability to meet default losses arising from multiple events of default. The cap is imposed on clearing members of Singapore Exchange Derivatives Clearing Limited (SGX-DC) and The Central Depository (Pte) Limited (CDP). The proposal

purports to limit a non-defaulting clearing member's liability to meet multiple default losses arising within a 30-day period to three times the aggregate of its funded and unfunded clearing fund contributions (prescribed contribution) as determined at the start of the 30-day period. The revised limit is intended to be independent of the clearing member's resignation. SGX has also proposed changes to the SGX-DC clearing rules set out in [Appendix B](#) of the consultation. SGX is seeking views and comments on: (1) capping the limit for multiple defaults at three times a clearing member's clearing fund contribution amount for all defaults occurring within a 30-day period; (2) the methodology for calculating the amount of a non-defaulting clearing member's clearing fund contributions available to meet losses suffered by the SGX central counterparty arising from or in connection with an event of default (as set out in SGX-DC Clearing Rule 7A.06.9.2); and (3) the rule amendments to effect the proposed change. The consultation closes on April 24, 2024. [NEW]

- **SFC and HKMA Further Consult on Enhancements to Hong Kong's OTC Derivatives Reporting Regime.** On March 22, 2024, the Securities and Futures Commission (SFC) and the Hong Kong Monetary Authority (HKMA) launched a [joint-further consultation](#) on enhancements to the over-the-counter (OTC) derivatives reporting regime in Hong Kong. This further consultation follows an earlier joint-consultation in April 2019, in which the SFC and HKMA proposed a requirement to identify transactions submitted to the Hong Kong Trade Repository (HKTR) for the reporting obligation by a Unique Transaction Identifier. The current joint-further consultation consults on the implementation of the Unique Transaction Identifier, together with the mandatory use of Unique Product Identifier and Critical Data Elements for submission of transactions to the HKTR. The Interested parties are encouraged to submit responses to the SFC or HKMA on the consultation by May 17, 2024.
- **ESMA Publishes Feedback on Shortening Settlement Cycle.** On March 21, the ESMA [published feedback](#) received to its Call for Evidence on shortening the settlement cycle in the EU. According to ESMA's report on the feedback, respondents focused on four areas: (1) many operational impacts, beyond adaptations of post-trade processes, were identified as the result of a reduction of the securities settlement cycle in the EU; (2) respondents identified a wide range of both potential costs and benefits of a shortened cycle, with some responses supporting a thorough impact assessment; (3) respondents provided suggestions around how and when a shorter settlement cycle could be achieved, with a strong demand for a clear signal from the regulatory front at the start of the work and clear coordination between regulators and the industry; and (4) stakeholders made clear the need for a proactive approach to adapt their own processes to the transition to T+1 in other jurisdictions. Additionally, according to ESMA, some responses warned about potential infringements due to the misalignment of the EU and North America settlement cycles.

New Industry-Led Developments

- **IOSCO Seeks Feedback on the Evolution of Market Structures and Proposed Good Practices.** On April 4, the International Organization of Securities Commissions (IOSCO) published a consultation report on [Evolution in the Operation, Governance and Business Models of Exchanges: Regulatory Implications and Good Practices](#). The consultation report analyzes the structural and organizational changes within exchanges, focusing on business models and ownership structures. It highlights a shift towards more competitive, cross-border, and diversified operations as exchanges integrate into larger corporate groups. The consultation report discusses regulatory considerations, particularly in the organization of individual exchanges and exchange groups and the supervision of multinational exchange groups. It addresses potential conflicts of interest arising from matrix structures and the challenges of overseeing individual exchanges within exchange groups. Additionally, it outlines a set of six proposed good

practices for regulators to consider in the supervision of exchanges, particularly when they provide multiple services and/or are part of an exchange group. The good practices are also complemented by a non-exclusive list of supervisory tools used by IOSCO jurisdictions to address the issues under discussion, in the form of “toolkits”. While the Consultation Report focuses on equities listing trading venues, the findings are also relevant to other trading venues, including non-listing trading venues and derivatives trading venues. IOSCO is seeking input from market participants on the major trends and risks observed, and the proposed good practices on or before July 3, 2024. [NEW]

- **ISDA Submits Response to CFTC Proposed Operational Resilience Rules.** On April 1, ISDA submitted [comments](#) on the CFTC’s notice of proposed rulemaking on requirements to establish an Operational Resilience Framework for Futures Commission Merchants, Swap Dealers and Major Swap Participants, which was published in the Federal Register on January 24, 2024. ISDA recommended that the CFTC adjust portions of the proposed rules relating to governance, third-party relationships, incident notification and implementation period. [NEW]
- **ISDA Submits Response to IOSCO Consultation on Post-Trade Risk Reduction.** On March 29, ISDA submitted a [response](#) to IOSCO consultation on post-trade risk reduction (PTRR) services. According to ISDA, PTRR services are intended to optimize bilateral and cleared derivatives portfolios to minimize the build-up of notional amounts and trade count, counterparty risk, and basis risk respectively, which in turn reduces systemic risk. ISDA stated that it is broadly supportive of IOSCO’s proposed sound practices. [NEW]
- **ISDA Submits Joint Response to PRA on Approach to Policy.** On March 28, ISDA and the Association for Financial Markets in Europe (AFME) submitted a joint [response](#) to the Prudential Regulation Authority (PRA) consultation on its approach to policy. The associations highlighted the importance of considering UK market specificities in meeting the secondary competitiveness and growth objective, and in the implementation of international standards. The associations expressed support for the continuation of structured policy development in dialogue with the industry, while also advocating for the enhancement of the PRA’s stakeholder engagement by re-establishing standing groups and horizon risk scanning groups, and greater industry cooperation during the initiation phase of the policy cycle. ISDA highlighted certain other points in the response, including recommendations on clustering regulatory principles and suggested improvements to the cost-benefit analysis and data collection processes to achieve greater transparency. [NEW]
- **ISDA Submits Joint Response to BCBS Crypto Standard Amendments Consultation.** On March 28, ISDA, with the Global Financial Markets Association, the Futures Industry Association, the Institute of International Finance and the Financial Services Forum, submitted a joint response to the Basel Committee on Banking Supervision (BCBS) consultation on proposed crypto asset standard amendments. ISDA and the other trade associations stated that they welcome the BCBS’s continued focus on designing and improving the prudential framework for crypto assets. The key topics in the consultation response include public permissionless blockchains, classification condition 2 and settlement finality and Group 1b eligibility.
- **ISDA Responds to CFTC on Clearing Member Funds Protection.** On March 18, ISDA responded to the CFTC’s consultation on proposed rules for the protection of clearing member funds held by derivatives clearing organizations (DCOs), including the assets of futures commission merchants (FCMs). According to ISDA, it proposed that the CFTC should finalize the enhanced protection for clearing member assets in connection with an intermediated DCO only, which includes multiple FCMs, unaffiliated with the DCO, as its members. Regarding a DCO providing direct clearing without multiple FCMs unaffiliated with the DCO, ISDA suggested the CFTC should wait to propose enhanced protection for clearing members’ assets, once a full assessment of the risks and complications

associated with a DCO providing direct clearing has been completed. At which point, in ISDA's opinion, it would be appropriate for the CFTC to propose a comprehensive framework to address these risks holistically. Otherwise, ISDA said, the current notice of proposed rulemaking would create a sense of safety for the disintermediated model, which is superficial due to the rule not creating a comprehensive safety regime for disintermediated central counterparties (CCPs), with many risks arising from such models being left unaddressed.

- **ISDA Responds to FASB on Induced Conversion of Convertible Debt.** On March 18, ISDA [submitted a response](#) to the Financial Accounting Standards Board's (FASB) exposure draft on File Reference No. 2023-ED600, Debt—Debt with Conversion and Other Options (Subtopic 470-20): Induced Conversions of Convertible Debt Instruments. ISDA indicated that it supports FASB's proposals in the exposure draft and believes it achieves the objective of improving the application and relevance of the induced conversion guidance to cash convertible debt instruments.

The following Gibson Dunn attorneys assisted in preparing this update: Jeffrey Steiner, Adam Lapidus, Marc Aaron Takagaki, Hayden McGovern, and Karin Thrasher. Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding these developments. Please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's Derivatives practice group, or the following practice leaders and authors: Jeffrey L. Steiner, Washington, D.C. (202.887.3632, jsteiner@gibsondunn.com) Michael D. Bopp, Washington, D.C. (202.955.8256, mbopp@gibsondunn.com) Michelle M. Kirschner, London (+44 (0)20 7071.4212, mkirschner@gibsondunn.com) Darius Mehraban, New York (212.351.2428, dmehraban@gibsondunn.com) Jason J. Cabral, New York (212.351.6267, jcabral@gibsondunn.com) Adam Lapidus – New York (+1 212.351.3869, alapidus@gibsondunn.com) Stephanie L. Brooker, Washington, D.C. (202.887.3502, sbrooker@gibsondunn.com) Roscoe Jones Jr., Washington, D.C. (202.887.3530, rjones@gibsondunn.com) William R. Hallatt, Hong Kong (+852 2214 3836, whallatt@gibsondunn.com) David P. Burns, Washington, D.C. (202.887.3786, dburns@gibsondunn.com) Marc Aaron Takagaki, New York (212.351.4028, mtakagaki@gibsondunn.com) Hayden K. McGovern, Dallas (214.698.3142, hmcgovern@gibsondunn.com) Karin Thrasher, Washington, D.C. (202.887.3712, kthrasher@gibsondunn.com) © 2024 Gibson, Dunn & Crutcher LLP. All rights reserved. For contact and other information, please visit us at www.gibsondunn.com. Attorney Advertising: These materials were prepared for general informational purposes only based on information available at the time of publication and are not intended as, do not constitute, and should not be relied upon as, legal advice or a legal opinion on any specific facts or circumstances. Gibson Dunn (and its affiliates, attorneys, and employees) shall not have any liability in connection with any use of these materials. The sharing of these materials does not establish an attorney-client relationship with the recipient and should not be relied upon as an alternative for advice from qualified counsel. Please note that facts and circumstances may vary, and prior results do not guarantee a similar outcome.

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