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Derivatives, Legislative and Regulatory Weekly Update (January 19, 2024)

Client Alert | January 19, 2024

From the Derivatives Practice Group: *Read below for global derivatives updates, including ISDA's response to US Basel III and G-SIB Surcharge.*

New Developments

- **CFTC Designates IMX Health, LLC as a Contract Market**. On January 18, the CFTC announced it has issued an Order of Designation to IMX Health, LLC, granting it designation as a contract market (DCM). IMX Health is a limited liability company registered in Delaware and headquartered in Chicago, Illinois. The CFTC issued the order under Section 5a of the Commodity Exchange Act (CEA) and CFTC Regulation 38.3(a). The CFTC determined IMX Health demonstrated its ability to comply with the CEA provisions and CFTC regulations applicable to DCMs. With the addition of IMX Health, there will be 17 DCMs. [NEW]
- **CFTC Issues Staff Letter No. 24-01**. On January 16, the CFTC issued Staff Letter No. 24-01, granting an exemption to LCH SA from the requirements of Regulation 1.49(d) to permit LCH SA to hold customer funds at the Banque du France. Additionally, the CFTC confirmed that it would not recommend enforcement action against LCH SA for failing to obtain, or provide the Commission with, an executed version of the template acknowledgment letter set forth in Appendix B to Regulation 1.20 , as required by Regulations 1.20(g)(4) and 22.5, for customer accounts maintained at the Banque de France. [NEW]
- **CFTC to Hold a Commission Open Meeting on January 22**. CFTC Chairman Rostin Behnam announced on January 12, 2024 that the Commission will hold an open meeting on Monday, January 22 at 9:30 a.m. (EST) at the CFTC's Washington, D.C. headquarters. The Commission will consider the following:
    - Notice of Proposed Order and Request for Comment on an Application for a Capital Comparability Determination Submitted on behalf of Nonbank Swap Dealers subject to Capital and Financial Reporting Requirements of the United Kingdom and Regulated by the United Kingdom Prudential Regulation Authority,
    - Proposed Rule: Requirements for Designated Contract Markets and Swap Execution Facilities Regarding Governance and the Mitigation of Conflicts of Interest Impacting Market Regulation Functions. [NEW]
- **SEC Publishes Risk Alert: Observations Related to Security-Based Swap Dealers**. On January 10, the SEC's Division of Examination published a Risk Alert presenting examination and outreach observations concerning compliance with rules applicable to security-based swap dealers. The SEC stated that in sharing these observations, the Division seeks to remind security-based swap dealers of their obligations under relevant security-based swap rules and encourage security-based swap dealers to consider improvements in their compliance programs, as may be appropriate, to further compliance with Exchange Act requirements. The Risk Alert presents observations in the following areas: (1) reporting of security-based swap transactions and correction of reporting errors; (2) business conduct

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standards; (3) security-based swap trading relationship documentation and portfolio reconciliation; and (4) recordkeeping.

- **CFTC Publishes Decentralized Finance Report**. On January 8, the CFTC's Digital Assets and Blockchain Technology Subcommittee of the Technology Advisory Committee (TAC) released a report entitled "Decentralized Finance." The report discusses TAC's view that the benefits and risks of DeFi depend significantly on the design and features of specific systems, and that one of its central concerns related to DeFi systems is the lack of, and some industry designs to avoid, clear lines of responsibility and accountability. TAC opined that this feature of DeFi systems may present the clearest ways in which DeFi poses risks to consumers and investors, as well as to financial stability, market integrity and illicit finance—according to TAC, it implicates no clear route to ensuring victim recourse, defense against illicit exploitation, or the ability to insert necessary changes and controls during periods of crisis and network stress. The report finds that government and industry should take timely action to work together, across regulatory and other strategic initiatives, to better understand DeFi.
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New Developments Outside the U.S.

- **RBI Issues Circular on Risk Management and Interbank Dealings**. On January 5, the Reserve Bank of India (RBI) issued a circular on risk management and interbank dealings. The RBI stated that it has reviewed the foreign exchange risk management facilities based on the feedback received from market participants and experience gained since the revised framework came into force. It has also consolidated the directions in respect of all types of foreign exchange transactions (including cash, tom and spot). The RBI explained that the directions contained in the Currency Futures (Reserve Bank) Directions, 2008 (Notification No. FED.1/DG(SG)-2008 dated August 06, 2008), and Exchange Traded Currency Options (Reserve Bank) Directions, 2010 (Notification No. FED.01/ED(HRK)-2010 dated July 30, 2010), as amended from time to time, are now being incorporated into the Master Direction – Risk Management and Inter-Bank Dealings. These

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revised directions will come into effect on April 5, 2024, replacing the existing directions in Part A (Section I) of the Master Direction – Risk Management and Inter-Bank Dealings dated July 5, 2016, as amended from time to time, superseding the notifications listed in Annex-II.

- **Hong Kong Consults on Regulatory Regime for Stablecoins**. On December 27, the Financial Services and the Treasury Bureau and the Hong Kong Monetary Authority (HKMA) jointly issued a public consultation paper on the legislative proposal for implementing the regulatory regime for stablecoin issuers in Hong Kong. Under the proposed regime, an issuer would be required to obtain a license from the HKMA if it issues a stablecoin that references the value of one or more fiat currencies in Hong Kong. The licensed issuer will have to fulfil certain financial resources requirements, and will be required to put in place an effective stabilization mechanism, such as maintaining a pool of high-quality and highly-liquid reserve assets with proper custody arrangement. The proposed regime further imposes governance, risk management and AML/CFT measures on licensees. Interested parties are encouraged to submit written comments on or before February 29, 2024.
- **ESAs Propose to Extend Equity Option Margin Exemption by Two Years**. On December 21, the European Supervisory Authorities (ESAs) – the European Securities and Markets Authority (ESMA), the European Banking Authority and the European Insurance and Occupational Pensions Authority – published draft regulatory technical standards (RTS) proposing a two-year extension (until January 4, 2026) to the exemption for equity options from bilateral margining under the European Market Infrastructure Regulation (EMIR). These RTS have to be endorsed by the European Commission and are subject to non-objection by the Council of the EU and the European Parliament before they enter into force. The draft RTS are accompanied by a statement from the ESAs that competent authorities "should not priorityse any supervisory or enforcement action" relating to bilateral margining for equity options until the entry into force of these amended RTS or the adoption of a long-term solution under EMIR 3, whichever occurs first."

New Industry-Led Developments

- **ISDA Launches Digital Version of 2002 ISDA Equity Derivatives Definitions**. On January 18, ISDA launched a fully digital edition of the 2002 ISDA Equity Derivatives Definitions on the ISDA MyLibrary platform, enabling new versions to be released more efficiently as products and market practices evolve in the future. Following consultation with buy- and sell-side market participants, ISDA identified support to move the definitions to a digital format, develop new product provisions and streamline certain components over time. Publication of the 2002 ISDA Equity Derivatives Definitions in digital form is a first step and enables further changes to be made in future versions. [NEW]
- **ISDA Launches Sustainability-linked Derivatives Clause Library**. On January 17, ISDA launched a clause library for sustainability-linked derivatives (SLDs), designed to provide standardized drafting options for market participants to use when negotiating SLD transactions with counterparties. SLDs embed a sustainability-linked cashflow in a derivatives structure and use key performance indicators (KPIs) to monitor compliance with environmental, social and governance (ESG) targets, incentivizing parties to meet their sustainability objectives. [NEW]
- **ISDA and SIFMA Response to US Basel III NPR**. On January 16, ISDA and the Securities Industry and Financial Markets Association (SIFMA) submitted a joint response on the US Basel III 'endgame' notice of proposed rulemaking (NPR). The response focuses on the Fundamental Review of the Trading Book (FRTB), the revised credit valuation adjustment (CVA) framework, the securities financing transactions requirements and elements of the standardized approach to counterparty credit risk rules. In the response, the associations propose a number

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of calibration changes to ensure the rules are appropriate and risk sensitive and avoid adverse consequences to US capital markets. [NEW]

- **ISDA and SIFMA Response to G-SIB Surcharge Framework Consultation**. On January 16, ISDA and the Securities Industry and Financial Markets Association (SIFMA) submitted a response to a consultation by the US Federal Reserve on proposed changes to the G-SIB surcharge. The response raises concerns that the revised G-SIB surcharge would lead to inappropriately high capital requirements for banks offering client clearing services, potentially discouraging them from participating in this business and contravening a long-standing policy objective to promote central clearing. Specifically, the response argues that client derivatives transactions cleared under the agency model should not be included in the complexity and interconnectedness categories of the G-SIB surcharge calculation. [NEW]
- **ISDA Updates OTC Derivatives Compliance Calendar**. On January 3, 2024, ISDA updated its global calendar of compliance deadlines and regulatory dates for the over-the-counter (OTC) derivatives space. The updated calendar can be found on the ISDA website.
- **ISDA Submits Response to HMT, FCA and PRA on UK EMIR**. On December 20, ISDA and UK Finance submitted a joint response to His Majesty's Treasury (HMT), the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) on the reform of the UK EMIR. ISDA stated that ISDA and UK Finance submitted the response in an attempt to inform the next stage of the UK's smarter regulatory framework reform package. In the response, the associations recommend a small number of clearly defined changes, seek certainty and permanence on current temporary exemptions and request an end to the current dependency on equivalence decisions for certain provisions (for instance, the intragroup exemption).

The following Gibson Dunn attorneys assisted in preparing this update: Jeffrey Steiner, Adam Lapidus, 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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