

OTC Derivatives Market Reforms

Progress report on Implementation

15 April 2011

Table of Contents

Implementation by jurisdictions and progress in international workstreams.....	1
Observations and next steps	4
ANNEX A Summary of responses to questionnaire on implementing OTC derivatives market reforms	8
ANNEX B Questionnaire on implementing OTC Derivatives Market Reforms.....	19

OTC Derivatives Market Reforms

Progress report on Implementation

In September 2009, G-20 Leaders agreed in Pittsburgh that:

All standardised OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements. We ask the FSB and its relevant members to assess regularly implementation and whether it is sufficient to improve transparency in the derivatives markets, mitigate systemic risk, and protect against market abuse.

In its October 2010 report on [Implementing OTC Derivatives Market Reforms](#) (the October Report), the FSB made 21 recommendations addressing practical issues that authorities may encounter in implementing the G-20 Leaders' commitments concerning standardisation, central clearing, exchange or electronic platform trading, and reporting of OTC derivatives transactions to trade repositories. At the November 2010 Seoul Summit, G-20 Leaders endorsed the FSB recommendations and asked the FSB to monitor OTC derivatives market reform progress regularly.

This is the first progress report by the FSB on OTC derivatives markets reform implementation. The body of this report is set out in two parts: (i) implementation by jurisdictions and progress in international bodies' workstreams; and (ii) overall observations on progress, including identification of issues meriting additional attention in the near term, and next steps.

The FSB notes that implementation is still in its early stages and that its next progress report to be delivered by October 2011 should provide greater insight into whether progress is on track. This report highlights a number of issues which will have a bearing on whether the G-20 commitments can be implemented in an internationally consistent manner by end-2012. The FSB notes its concern regarding many jurisdictions' likelihood of meeting the G-20 end-2012 deadline, and believes that in order for this target to be achieved, jurisdictions need to take substantial, concrete steps toward implementation immediately.

Implementation by jurisdictions and progress in international workstreams

January 2011 survey of FSB members

The FSB Secretariat conducted a survey in January 2011 of FSB members regarding their OTC derivatives market reforms implementation efforts. The responses show substantial variation across jurisdictions in the pace of implementing the recommendations in the October Report and the resulting progress toward achieving the G-20 commitments on standardisation, central clearing, exchange or electronic platform trading, and reporting to trade repositories. A summary of the survey responses prepared by the FSB Secretariat is attached as Annex A to this report.

In the largest, most developed OTC derivatives markets, major implementation projects are underway. In the United States, legislation has been enacted and implementing regulation is proceeding according to established timetables with respect to clearing, trading, and reporting to trade repositories (TRs); and in Japan, legislation has been enacted and implementing regulation is proceeding according to firm timetables with respect to clearing and reporting to trade repositories. In the European Union, legislation has been proposed and is expected to be adopted by end-2011 with respect to clearing and reporting to trade repositories, and is in the pre-proposal consultation stage regarding trading; while in Hong Kong the legal framework for a regulatory regime to govern an as-yet-to-be-established central counterparty (CCP) and trade repository is understood to be proposed during 2011.

In other markets with local or regional significance, there has been substantial policy analysis, but key legislative or regulatory next steps have yet to be taken. In Korea, the government has finalised plans for requiring mandatory central clearing, and a CCP is to be established by mid-2012. The government will propose legislation for approval by the Korean National Assembly in the second half of 2011. The Korean financial authority is also reviewing whether to establish a separate trade repository. In Canada, an inter-agency working group comprised of securities and prudential regulators, the finance ministry and the central bank has issued a report outlining key policy issues for the Canadian market; however, key decisions regarding whether to establish local infrastructure for clearing and transaction reporting or to rely on global infrastructure will be made in the course of 2011. Likewise in Australia, India, Mexico, Saudi Arabia, South Africa and Switzerland, financial authorities have embarked on an assessment of the derivatives markets operating within their jurisdictions and plan to decide upon future regulatory initiatives involving the implementation of the G-20 commitments in the course of 2011.

In some jurisdictions, while review of legislative and regulatory frameworks covering the spectrum of the G-20 commitments is ongoing, efforts have been made to introduce central clearing for OTC derivatives, but firm timetables for completion have not been established. In China, the central bank has required the use of standardised documentation and reporting to authorities of OTC derivatives transactions, and has promoted the establishment of a CCP to clear OTC derivatives. In Russia, legislation providing for central clearing of OTC derivatives was adopted in February 2011, while consideration of price transparency for OTC derivatives continues. The Indian central bank has developed the Clearing Corporation of India Limited to act as both CCP and trade repository in the Indian market, and has set up a working group to develop the modalities for a single-point reporting mechanism for all OTC interest rate and foreign exchange derivative transactions. It is intended to eventually clear all OTC derivatives transactions through the CCP. In Singapore, a preliminary industry consultation on the regulatory regime and market structure is underway; meanwhile, the Singapore Exchange already offers central clearing for OTC commodity derivatives, and, as of November 2010, for interest rate swaps.

Some jurisdictions have regulatory regimes covering derivatives that have been in place for some time. In Brazil, for example, it is estimated that approximately 90% of all derivatives are standardised, exchange traded and centrally cleared; since 1994, all OTC derivatives transactions are required to be registered with trade repositories that are self-regulatory organisations. While work is taking place to improve the quality of information reported to trade repositories, the Brazilian questionnaire response indicates that authorities there do not

see a need for a major legislative or regulatory initiative to achieve the G-20 commitments, given the highly standardised state of the market. In Argentina, bilaterally traded and settled derivatives comprise only about one-quarter of the market, as the other three-quarters of the market are centrally-cleared and either traded on exchange or on the Mercado Abierto Electrónico S.A. electronic platform, which is regulated by the Argentine market regulator.

In nascent markets, such as Indonesia and Turkey, consideration of approaches to implementing OTC derivatives market regulation is at an early stage.

FSB members also were asked whether the international workstreams underway covered the issues that need to be addressed to achieve full and internationally consistent implementation of the G-20 commitments by end-2012, and whether any emerging issues have been identified. While members were generally satisfied that the workstreams underway largely cover the appropriate issues, ongoing monitoring was seen to be key as implementation progresses further. The FSB considered the members' responses to these survey questions in developing the observations set out below.

International workstreams

In the October Report, the FSB recommended that appropriate international bodies with relevant expertise carry out needed work for the coordination of implementation of OTC derivatives market reforms in an internationally consistent and non-discriminatory way. Each of these international bodies has provided a report on progress achieved to date and its ongoing work.

The recommendations directed toward international bodies set out in the October Report are being undertaken through the following workstreams:

- BCBS work regarding the creation of incentives to centrally clear and higher capital charges for non-centrally cleared OTC derivatives (Basel III rule text published December 2010)¹ and the capitalisation of bank exposures to CCPs (consultative document published December 2010 and to be finalised during 2011)²
- CPSS-IOSCO review of standards for financial market infrastructures (consultation report published March 2011 and to be finalised by early 2012)³
- CPSS-IOSCO report on derivatives data and aggregation requirements for reporting to trade repositories (consultation report to be published in July 2011 and finalised by end-2011)
- CPSS-IOSCO guidance, to be developed in consultation with the OTC Derivatives Regulators' Forum (ODRF), on sound cross-border oversight arrangements for financial market infrastructures including CCPs (no timetable set)
- *IOSCO Report on Trading of OTC Derivatives* (published February 2011)⁴

¹ The Basel III rule text is available at: <http://www.bis.org/publ/bcbs189.pdf>

² The consultative document is available at: <http://www.bis.org/publ/bcbs190.pdf>.

³ The consultative document is available at: <http://www.bis.org/publ/cpss94.htm>.

⁴ The IOSCO Report on Trading of OTC Derivatives is available at: <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD345.pdf>.

- IOSCO report on international standards to address coordination of central clearing requirements with respect to products and participants (and any exemptions from clearing requirements) (report expected January 2012)⁵
- ODRF fostering development of cooperative frameworks for information sharing and cooperation among relevant authorities concerning individual OTC derivatives market infrastructures (ongoing)⁶
- OTC Derivatives Supervisors Group (ODSG) development of a roadmap and commitments covering standardisation, among other things, by G-14 dealers and other major market participants (commitment letter delivered 31 March 2011)⁷
- ODSG, working with standard setters, BIS, and other relevant authorities and market participants, development of reporting metrics to measure to what extent the recommendations in the October Report and G-20 commitments are being met (by July 2011)

Observations and next steps

Drawing on its consideration of the survey responses and progress reports by international bodies, the FSB has a number of observations concerning implementation progress generally, and more specifically addressing standardisation, central clearing, organised platform trading, and reporting to trade repositories.

General

A great deal of work has been undertaken at national, regional, and international levels toward implementation of OTC derivatives market reforms. However, although it is still early to be assessing progress toward implementing the G-20 commitments across jurisdictions, it must be noted that there are a number of jurisdictions that have not yet taken threshold decisions regarding the shape of the regulatory framework for their respective markets. The FSB notes its concern regarding many jurisdictions' likelihood of meeting the G-20 end-2012 deadline, and believes that in order for this target to be achieved, jurisdictions need to take substantial, concrete steps toward implementation immediately.

The FSB is concerned with the substantial variation across jurisdictions in the pace of implementation. Some jurisdictions expressed concern in their survey responses that implementation was proceeding too rapidly in some jurisdictions and too slowly in others. Another concern cited by some survey respondents was that the movement to central clearing was taking place before the issues related to the number and location of CCPs and TRs from a

⁵ Recommendation 12 notes that to minimize the potential for regulatory arbitrage, IOSCO, working with other authorities as appropriate, should coordinate the application of central clearing requirements on a product and participant level, and any exemptions from them.

⁶ Recommendation 21 notes that ODRF, working with CPSS and IOSCO, should continue to foster development of common frameworks for effective cooperation and coordination on oversight arrangements and information sharing among the relevant authorities for individual trade repositories and systemically important OTC derivatives CCPs.

⁷ The commitment letter is available at: <http://www.newyorkfed.org/newsevents/news/markets/2011/an110405.html>.

global perspective have been addressed. Some worried that the rushed pace of implementation might exacerbate, rather than mitigate, systemic risk.

The FSB believes a measured approach to consideration of new international workstreams to address emerging issues is warranted, as some fundamental work set out in the October Report recommendations is yet to be initiated or at a nascent stage. Accordingly, the FSB has specified below its observations on progress to date and the issues that are emerging as threshold issues or particularly timely.

Standardisation

The work that the ODSG has undertaken since 2005 was cited by several jurisdictions in their survey responses as key to increasing standardisation in the OTC derivatives market. Given the value of this work, authorities working with industry will continue to be crucial to achieving greater standardisation of contractual terms and operational processes.⁸ Therefore, whilst some have speculated that the ODSG's work in securing and monitoring commitments from G-14 dealers and buy-side participants may be unnecessary as regulatory regimes are established, the FSB supports the ODSG in continuing to work with G-14 dealers and other market participants, after establishing the 31 March 2011 roadmap, to ensure that targets set are achieved, and that future targets are developed as needed, consistent with regulatory frameworks established.

Central clearing

Different approaches to central clearing requirements appear to be emerging. The frameworks for central clearing in Japan, and United States and proposed in the European Union would provide for both "bottom up" and "top down" approaches,⁹ whilst some other jurisdictions have not yet decided whether to put in place a "top down" framework and currently rely on the "bottom up" approach alone. Monitoring efforts focused on the consistency of central clearing requirements will be critical. The IOSCO report on international standards addressing coordination of these requirements on the product and participant level, and any exemptions from clearing requirements, expected to be published in January 2012, will be important.

Some jurisdictions also consider the issues around CCP interoperability and access to CCPs for smaller and cross-border market participants as threshold issues bearing on the achievability of the G-20 commitment to central clearing by end-2012, as well as on the appropriate structure of derivatives markets. Inefficient access to clearing may reinforce the role of global systemically important financial institutions (SIFIs). To help explore these issues and determine appropriate next steps, the CGFS, CPSS, and IOSCO held a forum in January 2011 and are organising follow-up work to promote expanding access to central clearing to a broader set of participants, and links between CCPs, without sacrificing the

⁸ The ODSG work includes increasing both process and product standardisation through commitments for increased use of electronic processing and standard documentation. See http://www.newyorkfed.org/newsevents/otc_derivative.html.

⁹ The "bottom up" approach refers to a process through which contracts that a CCP proposes to clear are made subject to a mandatory clearing requirement by the relevant regulator. The "top down" approach means that the relevant regulator has the authority to identify OTC derivatives contracts that may be required to be cleared, irrespective of whether a CCP has yet proposed to clear them. Japan, the European Union and the United States have proposed frameworks that are not identical and differ with regard to particular constraints and authority that the relevant regulator has in taking regulatory actions.

rigour of CCP risk controls. Among other things, CPSS and IOSCO will conduct a stocktaking of current participant requirements for OTC derivatives CCPs, and the CGFS has established a study group to consider the macro-financial implications of CCP access and links. Other issues relating to CCPs that the official sector will need to consider further include oversight arrangements, access to central bank liquidity and resolution regimes.

The FSB believes that ensuring fair and open access to CCPs, subject to sound risk management, is essential for the G-20 objectives for OTC derivatives market reforms to be achieved.

Exchange or electronic platform trading

In February 2011, IOSCO published its *Report on Trading of OTC Derivatives*. The report marks progress toward clarifying the G-20 commitment to exchange or electronic platform trading, where appropriate, of standardised OTC derivatives. The report concludes that it is appropriate to trade standardised derivatives products with a suitable degree of liquidity on organised platforms, and that a flexible approach to defining what constitutes an organised platform would maximise the number of standardised derivatives products that can be appropriately traded on these venues. Additionally, the report identifies characteristics that organised platforms should exhibit in order to fulfil the G-20 Leaders' objectives of improving transparency, mitigating systemic risk, and protecting against market abuse in the derivatives markets.

The FSB notes that while IOSCO task force members were in agreement on seven of eight characteristics of organised platforms, task force members were not in full agreement as to whether organised platforms must provide platform participants with the opportunity to seek liquidity and trade with multiple liquidity providers within a centralised system in order to meet the G-20 objectives for the derivatives markets. The report recognises that if jurisdictions choose to establish trading requirements that differ in this aspect, the resulting regulatory disparities have the potential to influence market participants' choice of venues in which to conduct business. The FSB has requested that IOSCO undertake further analysis on market use of multi- or single-dealer platforms.

Reporting to trade repositories

Unless jurisdictions take approaches to trade reporting requirements that are consistent with the recommendations of the October Report, the FSB is concerned that the data collected on OTC derivatives transactions may not be able to be readily aggregated on a global basis and that authorities may not have effective and practical access. Survey responses revealed that some jurisdictions will require market participants to report OTC derivatives transactions to registered TRs, whilst others appear to consider reporting to governmental authorities, such as the central bank, sufficient.¹⁰

Survey responses also indicate questions regarding the depth and breadth of data that needs to be reported to trade repositories. Some have posited that a more limited data set is all that is needed for financial stability analysis. However, as discussed in the October Report, and confirmed by survey responses, authorities will rely on the data stored in trade repositories for

¹⁰ Recommendation 18 in the October Report states that reporting to the relevant authority would be appropriate in exceptional circumstances if it is not possible to report a particular transaction to a trade repository.

a variety of purposes. These purposes include financial stability analysis, monitoring of the use of non-standardised products, post-trade transparency, and market surveillance.

For data to be useful and provide global coverage of the derivatives markets, it will need to be reported and stored in a form that can be readily aggregated within and across repositories. In this regard, the reports of CPSS and IOSCO on data reporting standards and aggregation (consultation to be published in July 2011), as well as on standards for financial market infrastructures (consultation published in March 2011, which addresses regulator access to trade repository data including on a cross-border basis), will be important.

Survey responses indicate that only a few jurisdictions have undertaken work to identify barriers to the collection and dissemination of trade data by repositories and begun to take steps to address them. The FSB is concerned with this because, as noted in the October Report, such barriers may be more widespread. The FSB believes jurisdictions should undertake work to identify any such barriers in their jurisdiction and address them as a matter of urgency. To this end, the FSB supports further analysis and assessment of this issue as part of the ODSG commitment process through leverage of the work that already has completed in connection with that process.

Overall assessment

Although many jurisdictions have yet to make key decisions regarding the shape of their regulatory framework for OTC derivatives regulation, differences in approaches are emerging. Implementation of the 21 recommendations set out in the October Report is needed to promote consistency of OTC derivatives market reforms across jurisdictions, and the relevant authorities, standard setters and other groups should continue to work together to achieve this. Recognising that ultimately there likely will be a range of jurisdictional approaches taken, the FSB recommends that the focus in assessing progress going forward should be on: (i) assessing the degree to which the commitments and objectives set by the G-20 are being met; (ii) highlighting areas where coordination of future steps toward achieving G-20 objectives are needed; and (iii) flagging where differences in approaches may foster or facilitate opportunities for regulatory arbitrage or subject market participants and infrastructures to conflicting regulatory requirements.

Next steps

As a basis for the FSB's next progress report to be delivered by October 2011, the FSB secretariat plans to conduct a follow-up survey of FSB members in July. In addition to asking for a self-assessment of whether progress is on track to achieve the G-20 commitments by end-2012, the survey will seek to elicit detailed information on potential emerging issues.¹¹

Future progress reports also will use the reporting metrics being developed under the leadership of the ODSG as they become available and are applicable to assess the extent to which the recommendations of the October Report, and more generally, the G-20 commitments to central clearing, exchange or electronic platform trading, and reporting to trade repositories, are on the way to being achieved.

¹¹ Based on the survey results and progress reports, the FSB has preliminarily identified potential emerging issues such as backloading of existing contracts and phasing in of requirements; coverage of clearing requirements by asset class; implementation of the "top down" approach to central clearing requirements; and organised platform trading on multidealer versus single dealer platforms.

Summary of responses to questionnaire on implementing OTC derivatives market reforms

Introduction

In January 2011, FSB members were asked to complete a questionnaire¹² soliciting information on their respective jurisdictions' work plans and progress to date in implementing OTC derivatives market reforms, and in particular the recommendations set out in the In the October 2010 report on [Implementing OTC Derivatives Market Reforms](#) (the October Report). The questionnaire also provided an opportunity for member jurisdictions to identify any emerging issues or areas of where further guidance or international coordination may be necessary to achieve the G-20 commitments.

This note summarises the responses received from 25 jurisdictions.¹³

Implementation progress of OTC derivatives market reforms in member jurisdictions

General

Implementation progress to date varies substantially across jurisdictions. In the largest, most developed markets, major implementation projects are underway. In the United States, legislation has been enacted and implementing regulation is proceeding according to firm timetables with respect to clearing, trading, and reporting to trade repositories (TRs); and in Japan, legislation has been enacted and implementing regulation is proceeding according to established timetables with respect to clearing and reporting to TRs. In the European Union, legislation has been proposed and is expected to be adopted by end-2011 with respect to clearing and reporting to TRs, and is in the pre-proposal consultation stage regarding trading; while in Hong Kong the legal framework for a regulatory regime to govern an as-yet-to-be-established CCP and TR is understood to be proposed during 2011.

In other markets with local or regional significance, substantial policy analysis is underway, but key legislative or regulatory next steps have yet to be taken. In Korea, the government has finalised plans for requiring mandatory clearing, and a CCP is to be established by mid-2012. The government will propose legislation for approval by the Korean National Assembly in the second half of 2011. The Korean financial authority is also reviewing whether to establish a

¹² The questionnaire dated 5 January 2011 is attached as Annex B.

¹³ Argentina, Australia, Brazil, Canada, China, France, Germany, Hong Kong, India, Indonesia, Italy, Japan, Mexico, The Netherlands, Korea, Russia, Saudi Arabia, Singapore, South Africa, Spain, Switzerland, Turkey, United Kingdom, United States, and European Commission.

separate trade repository. In Canada, an inter-agency working group comprised of securities and prudential regulators, the finance ministry and the central bank has issued a report outlining key policy issues for the Canadian market; however, key decisions regarding whether to establish local infrastructure for clearing and transaction reporting or to rely on global infrastructure will be made in the course of 2011. Likewise in Australia, India, Mexico, Saudi Arabia, South Africa and Switzerland, financial authorities have embarked on an assessment of the derivatives markets operating within their jurisdictions and plan to decide upon future regulatory initiatives involving the implementation of the G-20 commitments in the course of 2011.

In some jurisdictions, efforts have been made to introduce central clearing for OTC derivatives, while review of legislative and regulatory frameworks covering the spectrum of the G-20 commitments is ongoing, but no firm timetables for completion have been set. In China, the central bank has required the use of standardised documentation and reporting to authorities of OTC derivatives transactions, and has promoted the establishment of a CCP to clear OTC derivatives. In Russia, legislation providing for central clearing of OTC derivatives was adopted in February 2011, while consideration of price transparency for OTC derivatives continues. The Indian central bank has developed the Clearing Corporation of India Limited (CCIL) to act as both CCP and TR in the Indian market, and has set up a working group to develop the modalities for a single-point reporting mechanism for all OTC interest rate and foreign exchange derivatives transactions. It is intended to eventually clear all OTC derivatives transactions through the CCP. In Singapore, a preliminary industry consultation on the regulatory regime and market structure is underway; meanwhile, the Singapore Exchange (SGX) already offers central clearing for OTC commodity derivatives, and, as of November 2010, for interest rate swaps.

Authorities in some smaller markets have not embarked on legislative or regulatory projects to implement OTC derivatives market reforms. Some jurisdictions have regulatory regimes covering derivatives that have been in place for some time. In Brazil, for example, it is estimated that approximately 90% of all derivatives are standardised, exchange traded and centrally cleared; since 1994, all OTC derivatives transactions are required to be registered with TRs that are self-regulatory organisations. While work is taking place to improve the quality of information reported to TRs, the Brazilian questionnaire response indicates that authorities there do not see a need for a major legislative or regulatory initiative to achieve the G-20 commitments, given the highly standardised state of the market. In Argentina, bilaterally traded and settled derivatives comprise only about one-quarter of the market, as the other three-quarters of the market are centrally-cleared and either traded on exchange or on the Mercado Abierto Electrónico S.A. (MAE) electronic platform, which is regulated by the Argentine market regulator.

In nascent markets, such as Indonesia and Turkey, consideration of approaches to implementing OTC derivatives market regulation is at an early stage.

Standardisation

Increasing standardisation of products and operational processes

The work of the OTC Derivatives Supervisors Group (ODSG) to secure commitments from the G-14 dealers, and certain buy-side institutions, and the work of ISDA to standardise contractual terms, was noted by ten¹⁴ of the 23 respondents as key to increasing standardisation in the OTC derivatives market.

Several jurisdictions noted other initiatives in their markets to increase standardisation of products and operational processes. China reported that its central bank is promoting the use of a standardised master agreement¹⁵ with standard definitions, and standardised internal processes including trade confirmation documentation and procedures. Hong Kong responded that it will continue to promote standardisation and consider how to increase the proportion of standardised derivatives in the market through consultation with an industry working group established under the Treasury Markets Association. Singapore noted that, to the extent bespoke OTC products traded in its market are similar to standardised products traded in major markets, its authorities would work with industry to increase standardisation in those products.

In the United States, operational standardisation will be required by regulation. The Dodd-Frank Act requires swap dealers and major swap participants to conform to such standards as may be prescribed by the CFTC and SEC regarding timely and accurate confirmation, processing, netting, documentation and valuation, and each agency has proposed rules for public comment. Russia noted that under legislation adopted in February 2011, its market regulator and central bank will promulgate regulations setting basic requirements for OTC derivatives standardisation.

Ensuring appropriate incentives for the use of standardised products

Many jurisdictions noted that implementation of the G-20 commitments to increase exchange or electronic platform trading, central clearing, and reporting to trade repositories of OTC derivatives transactions tend to lead to standardisation of OTC derivatives products and operational processes. Many respondents also indicated that introducing higher risk weights for non-centrally-cleared (and therefore non-standardised) OTC derivatives would provide the appropriate incentives for the use of standardised products.

South Africa highlighted the development of a new derivative product, known as a “Can-Do Option” traded on the Johannesburg Stock Exchange, which combines some elements of OTC and exchange trading and provides standardisation through an agreed valuation mechanism and greater transparency. Switzerland also highlighted the introduction of a trading facility for products known as collateralised secured investments or “COSI” on an affiliate of the SIX exchange in fall 2009. Like the Can-Do Options, the COSI products are only admitted to the platform if they adhere to predefined standards.

¹⁴ Australia, Canada, France, Germany, Hong Kong, Japan, Singapore, Switzerland, United Kingdom, United States, European Commission.

¹⁵ NAFMII Master Agreement (2009 version).

Mexico and Russia noted that in their jurisdictions the use of exchange-traded derivatives (which are, by definition, standardised) provides tax advantages not available for non-standardised OTC products.

Some jurisdictions responded that they have yet to conclude that increased standardisation beyond the current level would be needed in their respective markets to achieve the G-20 commitments. Australia noted that according to a recent industry survey, the Australian market already is well advanced in terms of legal standardisation, and that its regulators are currently exploring whether reporting metrics similar to those used in the G-14 dealer commitments would be useful in the Australian market. Likewise, Canada's interagency working group on OTC derivatives has gathered data on the Canadian market and is taking into consideration the work of the ODSG, with an aim to setting objectives and milestones in the first half of 2011. Saudi Arabia noted that a committee of Saudi banks is being established to study standardisation in this market, with a view to making recommendation on regulatory initiatives by end-2011.

Other jurisdictions cited already high levels of standardisation in their markets. Argentina and Brazil noted that trading in derivatives in their respective markets takes place in a far greater proportion in standardised, exchange-traded form (estimated at over 70% in Argentina, and approximately 90% in Brazil).¹⁶ India reported that the products currently traded OTC in its market are generally plain vanilla interest rate swaps and forward rate agreements covered by master agreements, and that CDS are proposed to be introduced as standardised products in line with international practice. India also noted that while the Indian market in foreign exchange derivatives has evolved substantially, it is still largely characterised by a limited range of functionally standardised forwards, swaps and plain vanilla European options, some of which are traded on-exchange. Saudi Arabia also noted the prevalence of the use of plain vanilla standardised products by its banks.¹⁷

Monitoring usage of non-standardised OTC derivatives products

Eight jurisdictions¹⁸ highlighted the future use of trade repositories, once developed, by supervisors and regulators to monitor usage of non-standardised derivatives.

Seven jurisdictions¹⁹ noted that they require frequent reporting of OTC derivatives trading by banks to the relevant supervisor.

Although most jurisdictions indicated that supervisors would monitor usage of non-standardised derivatives through the supervisory process, only a few jurisdictions provided any detail on how this would be accomplished or whether specific reporting requirements were in place. Argentina indicated that its central bank closely monitors usage of non-standardised OTC derivative products by requiring financial institutions to provide notes in

¹⁶ Brazil noted in its response that capital and credit risk management requirements, as well as requirements for institutional investors to centrally clear trades, can incentivize central clearing, which in turn can lead to greater standardisation

¹⁷ The Saudi Arabian Monetary Agency (SAMA) has required banks to use the standardised Customer Treasury Agreement (CTA), which is governed by Saudi law, with domestic customers since 2000. ISDA documentation, typically governed by English law, is used for international counterparties.

¹⁸ Brazil, Canada, Hong Kong, Japan, Mexico, Saudi Arabia, South Africa, Spain, European Commission. Brazil has an established TR that it already uses for monitoring purposes.

¹⁹ Argentina, China (reporting of non-electronic derivatives trades), India, Korea, Mexico and South Africa.

their quarterly financial statements regarding their usage of these products, and to include an annex²⁰ providing data on each financial instrument. This information is used as a basis for a semi-annual report on financial derivatives that the Argentine central bank publishes on its website. France indicated that its prudential supervisor for financial services institutions and insurance companies monitors the compliance of the largest banks with the ODSG commitments, including standardisation targets.

Central clearing

Moving to central clearing

Japan and the United States have enacted legislation requiring mandatory clearing of standardised OTC derivatives²¹ and are working on regulatory implementation of this requirement. The European Commission has proposed legislation requiring mandatory clearing of standardised derivatives that it expects to be enacted in 2011. Russia also adopted legislation in February 2011 regarding central clearing.²²

Several jurisdictions plan to make decisions concerning the structure of central clearing requirements for OTC derivatives in their markets during 2011. These include Australia, Canada, Hong Kong,²³ Mexico, South Africa, and Switzerland. Some jurisdictions²⁴ have initiated legislative or regulatory reviews in their jurisdictions to determine what central clearing requirements should apply, but did not set out any expected decision timeframe in their questionnaire responses.

Argentina and Brazil indicated in their questionnaire responses that they have no plans to introduce mandatory central clearing requirements in their respective jurisdictions, given the high level of standardisation, exchange and electronic platform trading and central clearing that already takes place in their markets.

Determining clearing eligibility

The frameworks for central clearing in Japan and in the United States, and the legislation proposed by the European Commission, provide for both “bottom up” and “top down” approaches to identifying the OTC derivatives required to be centrally cleared. The “bottom up” approach refers to a process through which contracts that a CCP proposes to clear are approved and then made subject to a mandatory clearing requirement by the relevant

²⁰ “Annex O.” See <http://www.bcra.gov.ar> →English version →Regulations →Updated Texts →Accounting Reporting System for quarterly/annual release.

²¹ In the case of Japan, actively traded OTC derivatives (such as plain vanilla interest rates swaps) will be required to be cleared on a domestic or foreign CCP; for derivatives where the clearing criteria closely relates to corporate bankruptcy criteria under Japanese law (such as the iTraxx Japan CDS) will be required to clear on a domestic CCP.

²² Federal Law N° 7-FZ “On clearing and clearing services” and Federal Law N° 8-FZ “On amendments to separate Russian legislative acts in connection with the adoption of the law on clearing and clearing services” were adopted on 7 February 2011.

²³ Hong Kong indicated that it will consult relevant stakeholders in 2011 with an aim of finalising its regulatory regime by end 2012.

²⁴ China, Saudi Arabia, Singapore, Turkey. Saudi Arabia indicated that a committee composed of domestic banks which is conducting a self-assessment regarding implementation of G-20 commitments will make recommendations by end-2011. Based on this, Saudi Arabia will make decisions regarding its regulatory framework.

regulator. The “top down” approach means that the relevant regulator has the power to identify OTC derivatives contracts that should be required to be cleared, irrespective of whether a CCP has yet proposed to clear them.

CCPs to clear OTC derivatives have been established, or are in the process of being established, in several jurisdictions in addition to those where mandatory clearing already has been adopted or proposed. These include Brazil, China (Shanghai Clearing House), Hong Kong, India (Clearing Corporation of India Limited or CCIL), and Singapore (AsiaClear). The availability of central clearing in these markets currently is determined using a bottom up approach.²⁵

Strengthening bilateral counterparty risk management

Implementation of strengthened bilateral counterparty risk management practices is taking place through a number of avenues and the questionnaire responses indicate good progress in this area.

In the European Union and United States, minimum bilateral counterparty risk management standards will be required by regulation. The European Commission proposal would require that all financial institutions and non-financial institutions above a certain threshold ensure that appropriate procedures are in place to measure, monitor, and mitigate operational risk. The draft legislation sets minimum requirements that must be met.²⁶ In the United States, the Dodd-Frank Act provides the CFTC, SEC, and the prudential regulators with rulemaking authority to address bilateral counterparty risk management. The CFTC has proposed rules to require swap dealers and major swap participants to meet certain requirements,²⁷ and continues to consider other rules.

Raising capital requirements on bilateral counterparty risk exposures, in particular through Basel III, was cited by several jurisdictions.²⁸

Four jurisdictions²⁹ cited efforts to standardise documentation in their markets to provide for close-out netting.

The ODSG and the commitments it has set for the G-14 dealers and certain buy-side participants also were identified by several members³⁰ as establishing targets for increasing the robustness of bilateral counterparty risk management.

²⁵ Hong Kong has indicated that both bottom up and top down types of mandatory clearing requirements are under consideration. India has been following both a top down approach to introduction of central clearing (e.g., for repo transactions in government securities) as well as a bottom up approach (e.g., foreign exchange forwards and interest rate swaps).

²⁶ These include: (i) the timely confirmation of the terms of the OTC derivatives contracts, where possible by electronic means, (ii) robust, resilient and auditable processes in order to reconcile portfolios, to manage associated risk and to identify disputes between parties early and resolve, and monitor the value of outstanding contracts, and (iii) timely, accurate and appropriately segregated exchange of collateral or the appropriate and proportionate holding of capital.

²⁷ These include: (i) participation in certain multilateral compression exercises, (ii) bilateral termination of all fully offsetting swaps by the close of business on the business days following the day the parties enters into the offsetting transaction; and (iii) annual engagement in bilateral portfolio compression exercises with counterparties that are also swap dealers or major swap participants.

²⁸ Canada, Netherlands, Russia, Singapore, Switzerland, United States.

²⁹ Brazil, China, Mexico, South Africa.

³⁰ Japan, United Kingdom, United States.

Three jurisdictions³¹ stated that authorities were conducting reviews of risk management guidelines for financial institutions.

Exchange or electronic platform trading

Promoting trading on organised platforms

The United States has taken a mandatory approach to trading on organised platforms. The Dodd-Frank Act requires any swap that is subject to a clearing requirement to be traded on a registered platform unless no registered trading platform makes such swap available to trade. The CFTC and SEC have proposed regulations and guidance which would apply to the registration and operation of swap execution facilities to implement the new statutory framework.

The European Commission has initiated a consultation as part of the review of the European Union Markets in Financial Instruments Directive (MiFID). The consultation envisages a mandatory requirement for trading on organised platforms for clearing-eligible derivatives that are deemed to meet certain additional criteria, including a sufficient level of liquidity. A legislative proposal is expected in the second quarter of 2011.

In Argentina, a regulation adopted in 2007 provides capital incentives for trading derivatives on an exchange or an electronic trading platform that also provides for guaranteed settlement.

Five jurisdictions³² noted that they would look to the IOSCO Report on Trading of OTC Derivatives as they review regulatory frameworks for their respective markets. Other jurisdictions³³ noted that they were conducting a review of policy options.

Both Argentina and Brazil indicated that they did not have plans to undertake legislative or regulatory initiatives to promote exchange and electronic platform trading, as a high percentage of the derivatives traded in their respective markets already trade on organised platforms. India indicated that exchange and electronic platform trading of OTC interest rate derivatives is not currently envisaged, as it takes the position that mandatory reporting through a centralised trade reporting platform, coupled with central clearing, will provide the benefits of exchange trading while retaining the flexibility of OTC transactions.

Exploration of increased price and volume transparency

Three jurisdictions³⁴ noted that trade repositories would play a key role in public disclosure of price and volume data regarding OTC derivatives transactions. In the United States, under authority provided by the Dodd-Frank Act, the CFTC and SEC have proposed regulations that would require post-trade price and volume transparency applicable to all derivatives transactions. These rules³⁵ would require transaction data to be reported to a trade repository,

³¹ Brazil, India, Korea. Brazil noted that formal legal requirements under Brazilian law, and likely for other civil law jurisdictions, for bilateral collateralisation need to be addressed to make bilateral collateralisation more efficient.

³² Australia, Canada, Hong Kong, Japan, Singapore.

³³ Canada, Korea, Mexico, Saudi Arabia.

³⁴ Japan, South Africa, United States.

³⁵ The categories of information to be reported would generally include, among other matters, asset class, underlying reference, price, notional amount, time of execution, effective date, and scheduled termination date.

and for the trade repository to disseminate certain information (including price and volume information) to the public in a timely manner.

The European Commission is consulting on a post-trade transparency regime, calibrated by asset class, as part of the MiFID review.

China noted that price, trade and aggregated market information about OTC derivatives transactions is made publicly available, and that greater transparency applies to electronically-traded OTC derivatives.

Two jurisdictions³⁶ noted that they have pre- and post-trade transparency regimes that apply to non-equity products. To the extent that OTC derivatives are traded on platforms falling within the applicability of the existing framework, the current pre- and post-trade transparency rules would apply.

Reporting to trade repositories

TR reporting requirements

The Japanese and US legislation, as well as the legislation proposed by the European Commission and Hong Kong, provides for mandatory reporting of OTC derivatives transactions to TRs. Australia, Canada, and Singapore indicated that they are considering the appropriate framework for implementing mandatory trade reporting and whether creation of a local TR will be necessary and/or reporting to global TRs will provide appropriate protections and access.³⁷ South Africa indicated that it will propose a local TR to be developed.

Several jurisdictions³⁸ already require reporting of OTC derivatives transactions to authorities. In certain cases, this takes place through a TR³⁹ or TR-like platform.⁴⁰ Mexico indicated that its authorities are considering whether to promote the development of a new TR, require reporting to global TRs, and/or strengthen the central bank database in which financial entities report their OTC derivatives transactions. The Indian central bank also is exploring the feasibility of requiring all foreign exchange and interest rate OTC derivatives transactions to be reported through the CCIL reporting platform.

Some jurisdictions⁴¹ that have not indicated that they have proposed or are contemplating mandatory reporting requirements for OTC transactions, currently provide for the recordation of transaction data concerning only exchange-traded products. Switzerland has indicated that based on conclusions regarding an ongoing study of the characteristics of Swiss OTC markets available in the second half of 2011, it will determine the direction of future regulatory initiatives.

³⁶ Italy, Switzerland.

³⁷ Hong Kong, which has proposed the establishment of a local TR, also noted it continues to consider issues around reporting to global TRs as it implements mandatory requirements.

³⁸ Argentina, Brazil, China, India, Korea, Mexico, Saudi Arabia. Russia requires reporting of registered open positions to the Federal Financial Markets Service (see footnote 42).

³⁹ Brazil.

⁴⁰ Argentina (OTC derivatives transactions traded on the electronic MAE platform); India, through the CCIL (currently limited in scope but may expand); China (reporting of certain asset classes through the electronic trading platform).

⁴¹ Indonesia, Switzerland.

Brazil noted that in addition to OTC derivatives transaction reporting, there is work underway in the private sector to create a central reporting mechanism for the aggregated derivatives positions of market participants.⁴²

Addressing data collection and dissemination

The legislation proposed by the European Commission addresses the barriers to the reporting of counterparty names to TRs for all submitting European Union entities. Canada, Hong Kong and Mexico indicated that legislative changes will be necessary to clarify confidentiality issues with respect to information sharing. No other jurisdiction indicated in its response that it is contemplating legislative changes to address barriers to data collection and dissemination. Switzerland noted its view that it is questionable whether a TR needs client information to strengthen financial stability.⁴³

The work of the ODSG in identifying the jurisdictions that need to modify their legislation to allow the reporting of client information to global TRs, and the development of potential interim solutions to the reporting of such information, was cited by several jurisdictions.⁴⁴ Other jurisdictions⁴⁵ conveyed their views of the importance of dealing with barriers to cross-border TR reporting and data aggregation.

Ensuring adequate access to data for the carrying out of regulatory mandates⁴⁶

Several jurisdictions⁴⁷ cited the work of the ODRF concerning cooperative oversight arrangements and information sharing by authorities.

In the United States, the Dodd-Frank Act requires that TRs must obtain the written agreement of the requesting authority to indemnify the TR and the CFTC or SEC before sharing data with foreign regulators. The SEC has indicated that it expects that a registered TR would not go beyond the minimum requirements set out in the statute.

Canada indicated that legislative changes will be necessary in its jurisdiction to ensure regulatory access and to clarify the terms of information sharing with and between TRs and regulators, including foreign regulators. Hong Kong also indicated that it would amend existing legislation and supervisory regulations to provide for a regulatory framework that facilitates timely access to the TR by regulators for supervisory purposes.

⁴² Through an initiative of BM&FBovespa, CETIP and Febraban, a non-profit “Derivatives Exposures Central” platform is being created to provide for access to counterparties to the aggregate derivatives positions held by Brazilian corporations that are registered with the exchange and/or the OTC markets. Russia also indicated that open positions in OTC derivatives pursuant to master agreements or which are centrally cleared are required to be registered with self-regulatory organizations and CCPs.

⁴³ Switzerland also noted that the two major Swiss market participants report OTC interest rate derivatives transactions to TriOptima, and that in this case the issue of data confidentiality “seems to be manageable” since the data is aggregated and does not directly expose the beneficiaries of the transaction.

⁴⁴ Japan, United Kingdom, United States.

⁴⁵ Germany, Hong Kong, Singapore.

⁴⁶ The FSB Secretariat notes that a number of jurisdictions appeared to interpret the question as querying whether access to data was adequate for the carrying out of *domestic* regulatory mandates, and did not provide any information on foreign regulatory access to domestic transactions data.

⁴⁷ Japan, Singapore, United Kingdom, United States.

International coordination of OTC derivatives market reforms

In general, questionnaire respondents were satisfied that the workstreams being undertaken by the appropriate international bodies identified in the October Report broadly cover the issues that need to be addressed to achieve full and internationally consistent implementation of the G-20 commitments to standardisation, central clearing, exchange or electronic platform trading, and reporting to trade repositories by end-2012.⁴⁸ A common theme was that ongoing monitoring of divergences in approaches was key as implementation progresses further and more detailed regulation is enacted.

Three areas identified by multiple questionnaire respondents as needing more attention were (i) CCP direct and indirect access and interoperability issues, (ii) TR issues, and (iii) consideration of sequencing issues and the pace of implementation.

CCP direct and indirect access and interoperability

Several jurisdictions cited concerns regarding access to CCPs for smaller and cross-border market participants. Respondents cited the CGFS-CPSS-IOSCO Access Forum meeting held on 21 January that initiated a discussion of these issues on an international level. Possible solutions to the access challenges could include ensuring broader risk-based direct access to global CCPs; building a system of local CCPs with linkages to larger or more global CCPs to avoid concentration of market power in the largest dealers and market fragmentation; and ensuring fair and secure indirect access to CCPs through client clearing.

Trade repositories

Several jurisdictions also cited concerns that existing workstreams may not be adequately addressing (i) the cross-border operation of trade repositories and the risk of global data fragmentation; (ii) elimination of legal barriers, such as client confidentiality provisions, to the collection and dissemination of data; (iii) regulatory access to TR data; and (iv) the use of repository data for financial stability purposes, including the development of centralised position reporting databases.

Sequencing and pace of implementation

In order to achieve implementation by end-2012, decisions need to be made about national frameworks and market structure for CCPs and TRs in the short term. Some jurisdictions have raised the concern that inefficient or inappropriate market structures could be chosen – potentially contrary to the goal of mitigating systemic risk – if threshold issues (for example, CCP access) are not addressed immediately. A concern was voiced that earlier implementation schedules in some jurisdictions are forcing decision-making in other jurisdictions. On the other hand, concern also was voiced about the adequacy of the pace of implementation across G-20 members. If some G-20 members do not meet their commitments to implement reforms by end-2012, opportunities for regulatory arbitrage and avoidance may be created.

⁴⁸ These workstreams are summarized in main text of the *FSB OTC Derivatives Market Reforms Progress Report on Implementation*.

Other issues

A number of other areas were highlighted by responding jurisdictions as emerging issues or areas that may merit international attention. These included:

- the regulatory arbitrage opportunities arising from differences in the stringency of TR reporting requirements and the definition of organised trading platforms;
- differences in bankruptcy regimes across jurisdictions and insolvency provisions applicable to OTC derivatives and CCPs;
- the risk of diversity in application of a mandatory clearing requirements particularly in the f asset class;
- consideration of the implications for emerging markets of implementation of the FSB recommendations in light of the size of OTC derivatives markets in these jurisdictions; and
- extraterritoriality concerns.

Implementing OTC Derivatives Market Reforms

Questionnaire

In September 2009, G-20 Leaders agreed in Pittsburgh that:

All standardised OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements. We ask the FSB and its relevant members to assess regularly implementation and whether it is sufficient to improve transparency in the derivatives markets, mitigate systemic risk, and protect against market abuse.

In the October 2010 report on [Implementing OTC Derivatives Market Reforms](#) (the “October Report”), the FSB made 21 recommendations addressing practical issues that authorities may encounter in implementing the G-20 Leaders’ commitments concerning standardisation, central clearing, exchange or electronic platform trading, and reporting of OTC derivatives transactions to trade repositories. In Seoul, G20 Leaders endorsed the FSB recommendations and asked the FSB to monitor OTC derivatives market reform progress regularly.

The objectives of this questionnaire are to solicit information on FSB member jurisdictions’ work plans and progress to date in implementing OTC derivatives market reforms, and in particular the recommendations set out in the October Report, as well as to provide an opportunity for member jurisdictions to identify any emerging issues or areas of where further guidance or international coordination may be necessary to achieve the G-20 commitments. Responses to this questionnaire will be considered by the FSB OTC Derivatives Working Group, which will provide a progress report to the FSB in March 2011 covering implementation efforts in member jurisdictions as well as coordination in international workstreams. In addition, the responses will be used by the FSB in preparing its report on progress to the G20 expected in April 2011.

Member jurisdictions are requested to provide a consolidated jurisdictional response to the questionnaire, covering all supervisors and regulators responsible for implementing OTC derivatives market reforms. Please ensure answers are brief and respond directly to the relevant questions.

Responses will be posted on the FSB internal website for member's information, but will not be published.

Member jurisdictions are kindly requested to return the completed questionnaire to the FSB Secretariat (sarahcasey.otte@bis.org) by close of business on Monday, 31 January 2011.

1. Implementation progress of OTC derivatives market reforms in member jurisdictions

1.1 *General.* Have legislative, regulatory and/or supervisory projects been initiated in your jurisdiction to implement the G-20 commitments to OTC derivatives standardisation, central clearing, exchange or electronic platform trading, and reporting to trade repositories?

- What key milestones have been set in your jurisdiction to achieve implementation by end-2012?
- Please identify any areas where follow-up or additional work is needed to implement the recommendations made by the FSB in the October Report.

1.2 *Standardisation.* With regard to increasing OTC derivatives' standardisation (see recommendations 1-4 of the October Report), has implementation been initiated in your jurisdiction?

- What work is being done to increase standardisation of contractual terms? How are standardised operational processes being promoted?
- How is work proceeding in your jurisdiction to ensure appropriate incentives for the use of standardised products?
- How will usage of non-standardised OTC derivatives products be monitored in your jurisdiction?
- What further implementation work remains with regarding to increasing standardisation?
- What key milestones have been set?

1.3 *Central clearing.* With regard to moving to central clearing of OTC derivatives (see recommendations 5-12 of the October Report), has implementation been initiated in your jurisdiction?

- How will it be determined whether a product is standardised and therefore should be centrally cleared?
- How is work proceeding on strengthening bilateral counterparty risk management of OTC derivatives that are not centrally cleared?
- What further implementation work remains with regard to central clearing?
- What key milestones have been set?

1.4 *Exchange or electronic platform trading.* With regard to promoting trading on exchanges or electronic trading platforms of standardised derivatives, where appropriate (see recommendations 13-14 of the October Report), has implementation been initiated in your jurisdiction?

- What work is underway to consider price and volume transparency?
- What further implementation work remains with regard to exchange or electronic platform trading?
- What key milestones have been set?

1.5 *Reporting to trade repositories.* With regard to reporting to trade repositories of OTC derivatives (see recommendations 15-19 of the October Report), has implementation in your jurisdiction been initiated with regard to requiring reporting of transactions to trade repositories by end-2012?

- What work is underway to address legal barriers to data collection and dissemination by trade repositories, including addressing client confidentiality issues?
- What work is underway to ensure different official sector bodies' adequate access to data that they require to carry out their respective regulatory mandates?
- What further implementation work remains with regard to reporting to trade repositories?
- What key milestones have been set?

2. International coordination of OTC derivatives market reforms

2.1 A number of workstreams are in train to coordinate implementation of OTC derivatives market reforms (see FSB secretariat note on *Taking forward work on OTC derivatives dated 4 January*). In the view of your jurisdiction, do these workstreams cover the issues that need to be addressed to achieve full and internationally consistent implementation of the G-20 commitments to standardisation, central clearing, exchange or electronic platform trading, and reporting to trade repositories by end-2012? If not, what additional work is needed, and on what timeframe?

2.2 Have any emerging issues been identified by your jurisdiction that could increase the potential for regulatory arbitrage or otherwise hamper the ability to achieve international implementation of the recommendations? If so, please specify whether your jurisdiction believes that such issues are adequately addressed by the workstreams in train, or, if additional work is needed, what should be covered and on what timeframe.