GIBSON DUNN

This Week in Derivatives

July 26, 2024

From the Derivatives Practice Group: ISDA released their Document Negotiation Survey, which found that the average time taken to negotiate key derivatives documents hasn't fallen since 2006.

New Developments

- **CFTC Staff Issues No-Action Letter Regarding Reporting and Recordkeeping Requirements for Fully Collateralized Binary Options.** On July 12, the CFTC announced the Division of Market Oversight and the Division of Clearing and Risk have taken a no-action position regarding swap data reporting and recordkeeping regulations in response to a request from ForecastEx LLC, a designated contract market and derivatives clearing organization. The divisions will not recommend the Commission initiate an enforcement action against ForecastEx or its participants for certain swap-related recordkeeping requirements and for failure to report data associated with binary option transactions executed on or subject to the rules of ForecastEx to swap data repositories. [NEW]

- **President Biden Announced Intent to Nominate Julie Brinn Siegel as a Commissioner of the CFTC.** On July 11, President Biden announced his intent to nominate Julie Brinn Siegel to be a Commissioner of the CFTC. Siegel currently serves as the federal government's deputy chief operating officer as Senior Coordinator for Management at the Office of Management and Budget (OMB). Prior to that, Siegel served as Secretary of the Treasury Janet Yellen's Deputy Chief of Staff and served as Senior Counsel and Policy Advisor to U.S. Senator Elizabeth Warren (D-MA). Last month, President Biden nominated CFTC Commissioner Johnson to be Assistant Secretary for Financial Institutions at the Department of Treasury and nominated CFTC Commissioner

Christy Goldsmith Romero to be Chair and Member of the Federal Deposit Insurance Corporation (FDIC) which, if confirmed by the Senate, would leave open two Democratic Commissioner seats at the CFTC. Siegel, if nominated and confirmed by the Senate, would take the seat of Commissioner Goldsmith Romero.

- **First Interagency Fraud Disruption Conference Focuses on Combatting Crypto Schemes Commonly Known as "Pig Butchering."** On July 11, the CFTC and the DOJ's Computer Crime and Intellectual Property Section's National Cryptocurrency Enforcement Team ("NCET") convened the first Fraud Disruption Conference to work on efforts to combat a type of fraud commonly known as "pig butchering." It is estimated that Americans are scammed out of billions per year, making this a top law enforcement priority. The working group addressed strategies to prevent victimization; using technology to disrupt the fraud; and collaboration on enforcement efforts. Several agencies also collaborated on an anti-victimization messaging campaign to warn Americans to remain vigilant against emerging fraud threats.

New Developments Outside the U.S.

- **ESAs Publish Joint Final Report on the Draft Technical Standards on Subcontracting under DORA.** On July 26, the European Supervisory Authorities published their joint Final Report on the draft Regulatory Technical Standards ("RTS") specifying how to determine and assess the conditions for subcontracting information and communication technology ("ICT") services that support critical or important functions under the Digital Operational Resilience Act ("DORA"). These RTS aim to enhance the digital operational resilience of the EU financial sector by strengthening the financial entities' ICT risk management over the use of subcontracting. [NEW]

- **ESMA Sets Out Its Long Term Vision on the Functioning of the Sustainable Finance Framework.** On July 24, ESMA published an Opinion on the Sustainable Finance Regulatory Framework, setting out possible long-term improvements. ESMA considers that, in the longer-term, the Framework could further evolve to facilitate investors' access to sustainable investments and support the effective functioning of the Sustainable Investment Value Chain. The opinion recommends several action items, including that all financial products should disclose some minimum basic sustainability information, covering environmental and social characteristics, and a product categorization system, based on a set of clear eligibility criteria and binding transparency obligations. [NEW]

- **ESAs Establish Framework to Strengthen Coordination in Case of Systemic Cyber Incidents.** On July 17, the ESAs announced they will establish the EU systemic cyber incident coordination framework ("EU-SCICF"), in the context of the Digital Operational Resilience Act ("DORA"), that will aim to facilitate an effective financial sector response to a cyber incident that poses a risk to financial stability, by strengthening the coordination among financial authorities and other relevant bodies in the European Union, as well as with key actors at international level.

- **ESAs Publish Second Batch of Policy Products under DORA.** On July 17, the ESAs published the second batch of policy products under DORA. This batch consists of four final draft regulatory technical standards, one set of Implementing Technical Standards and 2 guidelines, all of which aim at enhancing the digital operational resilience of the EU's financial sector.

- **Hong Kong HKMA and FSTB Publishes Results from Stablecoin Consultation.** On July 17, 2024, the Hong Kong Monetary Authority ("HKMA") and Financial Services and the Treasury Bureau ("FSTB") published the Consultation Conclusions on the Legislative Proposal to Implement the Regulatory Regime for Stablecoin Issuers in Hong Kong ("Consultation Conclusions"). The Consultation Conclusions outlined the legislative proposal to implement a regulatory regime for fiat-referenced stablecoin ("FRS") issuers in Hong Kong. The regime will primarily focus on representations of value which rest on ledgers that are operated in a decentralized manner in which no person has the unilateral authority to control or materially alter its functionality or operation. Under this regime, FRS issuers will require a license. Foreign entities intending to apply for a license will be required to establish a Hong Kong subsidiary and have key management personnel in the territory. [NEW]

- **ESMA Consults on Firms' Order Execution Policies Under MiFID II.** On July 16, ESMA launched a consultation on draft technical standards specifying the criteria for how investment firms establish and assess the effectiveness of their order execution policies. The objective of the proposed technical standards is to foster investor protection by enhancing investment firms' order execution. [NEW]

- **ESMA Publishes 2023 Data on Cross-Border Investment Activity of Firms.** On July 15, ESMA announced they completed an analysis of the cross-border provision of investment services during 2023. The main findings include that a total of around 386 firms provided services to retail clients on a cross-border basis in 2023; compared to 2022, the cross-border market for investment services grew by 1.6% in terms of firm numbers, and by 5% in terms of retail clients, while the number of complaints increased by 31%; and Germany, France, Spain, and Italy are the most significant destinations (in terms of number of retail clients) for investment firms providing cross-border services in other Member States. [NEW]

- **ESAs Consult on Guidelines under the Markets in Crypto-Assets Regulation.** On July 12, the ESAs published a consultation paper on Guidelines under Markets in Crypto-assets Regulation ("MiCA"), establishing templates for explanations and legal opinions regarding the classification of crypto-assets along with a standardized test to foster a common approach to classification.

- **ESAs Report on the Use of Behavioral Insights in Supervisory and Policy Work.** On July 11, the ESAs published a joint report following their workshop on the use of behavioral insights by supervisory authorities in their day-to-day oversight and policy work. The report provides a high-level overview of the main topics discussed during the workshop held in February 2024 for national supervisors and other competent authorities, where participants explored the added value of behavioral insights in their work by exchanging their experiences and discussing the challenges they face.

- **ESMA Publishes the 2024 ESEF Reporting Manual.** On July 11, ESMA published the update of its Reporting Manual on the European Single Electronic Format ("ESEF") supporting a harmonized approach for the preparation of annual financial reports. ESMA has also updated the Annex II of the Regulatory Technical Standards ("RTS") on ESEF.

New Industry-Led Developments

- **ISDA Survey Shows Need for Greater Efficiency and Automation in Document Negotiation.** ISDA has published its survey on document negotiation, which shows the average time taken to negotiate key derivatives documents hasn't fallen since 2006, with some negotiations taking longer due to resource constraints, regulatory pressures and operational challenges. The ISDA Document Negotiation Survey collects and reports data on the composition, negotiation and digital automation of ISDA documentation. The results are based on responses from 42 institutions, most of which are banks or broker-dealers. [NEW]

- **ISDA Submits Letter to IASB on Contracts for Renewable Electricity.** On July 17, ISDA submitted a comment letter to the International Accounting Standards Board ("IASB") in response to its exposure draft, which seeks to address the accounting matters related to renewable electricity contracts and the impact on hedge accounting. ISDA provided additional information and proposed other instances, in addition to contracts for renewable electricity, where ISDA believes that hedge accounting with a variable notional should be permitted, such as balance guaranteed swaps. [NEW]

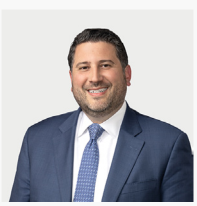
- **ISDA Publishes Response to Bank of England and Financial Conduct Authority on UK EMIR Refit.** On July 23, ISDA responded to a consultation from the Bank of England ("BoE") and Financial Conduct Authority ("FCA") on the additional draft Q&A for position-level reporting of spread bets under the UK European Market Infrastructure Regulation ("UK EMIR") Refit. In the response, ISDA agreed with the proposal to require reporting of spread bets at position level only, while highlighting that ISDA thinks that the requirement for all derivatives to be reported at the trade level, and the mutual agreement needed between parties for position-level reporting to occur.

- **ISDA Publishes Whitepaper: Hedge Accounting Under US GAAP.** On July 16, ISDA published a whitepaper that explores the issues faced by financial and non-financial institutions in applying hedge accounting for interest rate risk, foreign exchange risk and other risks. It highlights both the prescriptive nature of Accounting Standards Codification 815 and the inconsistent interpretations among auditors, which together create operational burdens and can limit hedging strategies. The paper proposes potential solutions to these challenges, including the expansion of hedge eligibility and the revision of hedge accounting criteria, to allow better use of existing risk management tools.

- **ISDA and SIFMA Submit Addendum on GIRR Curvature to US Basel III NPR.** On July 15, ISDA and the Securities Industry and Financial Markets Association ("SIFMA") submitted an addendum to the joint US Basel III "endgame" notice of proposed rulemaking. The addendum contains a proposal for general interest rate risk ("GIRR") curvature to fix an issue that was recently identified.

- **ISDA Chief Executive Officer Scott O'Malia Offers Informal Comments on Terminating Derivatives Contracts.** On July 15, ISDA CEO Scott O'Malia opined on the process to terminate a derivatives contract. ISDA is developing wo initiatives – the ISDA Close-out Framework and the ISDA Notices Hub – that will help ensure a key part of the termination process is more efficient. The ISDA Close-out Framework is designed to illustrate the various steps and decisions firms need to take and is intended as a preparatory tool for future stress events. The ISDA Notices Hub allows the instantaneous delivery and receipt of notices via a secure online platform, eliminating risk exposures and potential losses that can result from delays in terminating derivatives contracts.

Practice Group Members



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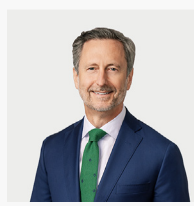

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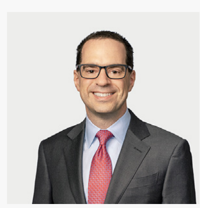

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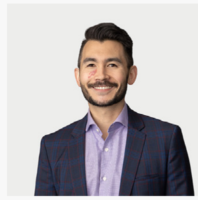

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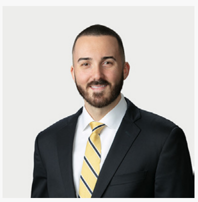

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