Increasing Market Efficiency: Issues Specific to Derivatives

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Food for Thought

“You can have data without information, but you cannot have information without data.”
– Daniel Keys Moran

“The goal is to turn data into information, and information into insight.”
– Carly Fiorina

“In God we trust. All others must bring data.”
– W. Edwards Deming
Looking Back

• What are the objectives of the G20 mandates?
  – Greater regulatory transparency
    G20 Pittsburgh 2009 Communique:
    “OTC derivative contracts should be reported to trade repositories...to improve transparency in the
derivatives markets, mitigate systemic risk and protect against market abuse.”
  – Mitigation of systemic risk
  – Protecting against market abuse

• Over the past several years, much work has been undertaken to achieve the transparency objective:
  – Multiple reporting regulations issued across jurisdictions - some as a big-bang go-live, some staggered
  – Trade repositories established and receiving trade reports
  – Industry reporting processes implemented

• Transparency is unquestionably better now than before the crisis.
  – Today, the vast majority of OTC derivatives trades are in fact reported, and additional jurisdictions are still
going live (for additional types of reporting entity and/or asset class)
Where Are We Now?

- Despite this seeming progress, major challenges remain:
  - Different, duplicative, conflicting and non-standardised reporting requirements across jurisdictions
  - Some data requirements are not clearly defined
  - The availability of ‘substituted compliance’ for reporting is limited, adding to duplication
  - Standardized reporting formats have been not adopted quickly or broadly enough
  - There is a lack of agreement as to how some data reporting requirements should be standardized across jurisdictions
  - Regulatory endorsement of standards already in use has been limited
  - Some reporting regimes are ‘closed markets’ – meaning they have their own trade repositories which do not leverage international standards and mechanisms
  - Legal barriers exist to sharing data and information, both within and across borders
  - Trade repositories have their own unique data architectures, formats and methods of sharing information
  - There is no facilitator or mechanism to aggregate data from different trade repositories globally
  - There is a lack of commitment among stakeholders in the process to drive and achieve consensus in these areas
Where Are We Now?

• As a result of these obstacles:
  – Regulators continue to lack a true picture of risk in individual jurisdictions because of incomplete and inconsistent trade data. On a global level, this means that efforts to aggregate data (and risk exposures) remain little more than a dream.
  – Market participants face costly, duplicative and conflicting trade reporting rules.
  – Trade repositories have the unenviable task of collecting and standardizing data from multiple sources for multiple jurisdictions.

• Fortunately, all of these issues have solutions, however they will require the active support and cooperation of a range of global stakeholders – regulators, market participants and infrastructure providers.

• Now that major jurisdictions have largely implemented their reporting regimes, national regulators are increasingly turning their minds to cross-border efforts to achieve regulatory consistency as much as possible.
International Coordination to Date

• Trying to address issues such as:
  – Duplicative reporting: long-term, global solution needed
  – Collateral reporting: jurisdictional differences
  – Consistency of data field population
  – Jurisdiction-specific constructs and idiosyncratic ("outlier") requirements

• CPMI-IOSCO Data Harmonisation Group formation:
  – Sept 2014: FSB Feasibility Study on approaches to aggregate OTC data
  – Nov 2014: CPMI-IOSCO establishes working group for harmonisation of key OTC derivatives data elements (Harmonisation Group)
  – Mandate is to develop guidance regarding definition, format, usage
  – Encourages use of internationally-agreed global standards for reporting
  – Includes (but not limited to) ECB, ESMA, CFTC, SEC, Federal Reserve Board, AMF, OSC, CSRC, BaFin, HKMA, JFSA, BoE, FCA
International Coordination to Date (cont’d)

• Legislative barriers to reporting (blocking statutes):
  – Legislation in some jurisdictions completely prohibits counterparty identification, even if counterparty does consent

• Restrictions on use of data mean that cross-border access to data remains a challenge:
  – MoUs usually a prerequisite to access to foreign TR data relevant to a domestic regulator’s mandate
  – However, legal barriers and lack of indemnification provisions still exist, precluding regulators from cross-border data access
  – Access may only be available to a primary authority (eg; securities regulator) but not to a non-primary authority (eg; prudential regulator, central bank)
  – Even when access is permitted, it may only be indirect access via the foreign regulator (not direct access to the foreign TR)

• Globally coordinated work is now underway to address this:
  – FSB Aug 2016 Report on FSB Members’ Plans to Address Legal Barriers to Reporting and Accessing OTC Derivatives Data
  – Commits FSB member jurisdictions to remove legislative barriers by mid-2018
  – Recommends ‘masking’ of new transactions be discontinued by end-2018 once barriers to reporting are removed
  – Only covers FSB members, yet some FSB non-member jurisdictions still have blocking statutes in place
What We Need: The Roadmap

• To truly reach the ultimate goal of a single, globally-harmonised, high-quality data set which regulators can use to meet the G20 objectives and improve risk monitoring, a number of improvements to existing reporting regimes need to be made:
  – Harmonised, consistent reporting requirements, within and across jurisdictions
  – Removal of barriers to sharing data & information between regulators
  – Global promotion, regulatory endorsement, adoption and convergence on common data standards and formats
  – Greater availability of substituted compliance
  – Interconnectivity and interoperability between trade repositories
  – Greater cross-border regulatory focus on global aggregation mechanisms
  – Designation of jurisdictional, regional and global leaders to spearhead the aggregation effort

  – These issues cannot be solved at the individual jurisdiction level, and require global collaboration, coordination and engagement
  – Only through implementing the above prerequisites can the goal of transparency truly be achieved
Usefulness of a Global Data Set

• Assessing systemic risk
  – Collecting and sharing global aggregated data
  – Examining size
  – Examining concentration
  – Examining interconnectedness
  – Examining structure
  – Evaluating derivatives for central clearing / platform trading determinations

• General macro assessment

• Monitoring trading activity, market surveillance and enforcement
  – Monitoring physical deliveries
  – Detecting market / price manipulation
  – Detecting insider trading, wash trading, market rigging, front-running
Usefulness of a Global Data Set (cont’d)

• Supervising market participants
  – Registering / regulating participants
  – Business conduct
  – Prudential supervision
• Regulating, supervising and overseeing market infrastructures
  – Trading venues (exchanges, platforms, markets)
  – CCPs
  – Payment systems
• Planning and conducting resolution activities
• Implementing monetary policy / lender of last resort function
  – Managing currency policy and exchange controls
  – Implementing monetary policy
  – Acting as lender of last resort
THANK YOU