17 February 2021

Dear Sir / Madam,

**Re: Commission Draft Equivalence Decisions for Australia, Brazil, Canada, Hong Kong, Singapore and the US Prudential Regulators**

The International Swaps and Derivatives Association, Inc. (**ISDA**)[1] welcomes the opportunity to comment on the proposed Commission Implementing Decisions (**Proposed Equivalence Decisions**) on recognition of the legal, supervisory and enforcement arrangements of Australia, Brazil, Canada, Hong Kong, Singapore and the US Prudential Regulators as equivalent to the valuation, dispute resolution and margin requirements of Article 11 of Regulation (EU) No 648/2012 of the European Parliament and Council on OTC derivatives, central counterparties and trade repositories (**EMIR**).

We set out below, for each jurisdiction, our detailed comments on the individual Proposed Equivalence Decisions. The Decision which is of greatest interest to ISDA members is that in respect of the US Prudential Regulators, for which we have concerns about the current drafting which would limit its practical use by EU firms. We have included some proposed drafting changes intended to overcome these limitations while continuing to satisfy the underlying policy objectives.

## 1. General comments

ISDA has two general comments in relation to the Proposed Equivalence Decisions on which we would welcome clarification from the Commission. While these may not be points that can be addressed in the Proposed Equivalence Decisions themselves, these are key points for ISDA members and we would be grateful if they could be addressed through guidance or Q&A:

- **Requirement under Article 13 EMIR for at least one of the counterparties to be "established" in the relevant third country**: Article 13 EMIR provides that an implementing act on equivalence shall imply that counterparties entering into a transaction subject to EMIR shall be deemed to have fulfilled the obligations contained in Articles 4, 9, 10 and 11 where at least one of the counterparties is established in that third country. We understand that in this context "established" means "incorporated in"

[1] **About ISDA**
Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 925 member institutions from 74 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter, LinkedIn, Facebook and YouTube.

the relevant jurisdiction. However, while the margin obligation under EMIR applies to FCs and NFCs established in the EU (and would not apply to OTC derivative contracts entered into between entities that are not established in the EU, unless the contracts are considered to have a direct, substantial and foreseeable effect within the EU), this is not always the case for other jurisdictions. In some cases an EU counterparty may enter into an OTC derivatives transaction that is subject both to the margin obligation under EMIR and also to the margin obligation of a third country, even though neither counterparty is "established" in the relevant third country. For example, this may be the case in relation to the US, where counterparties may be subject to requirements under the rules of the US authorities (including the CFTC and the Prudential Regulators) without being "established" in the US. We would welcome confirmation from the Commission that an EU firm may rely on the exemption in Article 13 (and on other exemptions which cross-refer to the equivalence decision under Article 13) where at least one counterparty is subject to the rules of the relevant third country even if neither counterparty is "established" in that third country.

- **Conditional equivalence decisions**: ISDA appreciates that the Commission is seeking to take a flexible approach to granting equivalence decisions in relation to jurisdictions which may not yet have introduced obligations equivalent to those in all of Articles 4, 9, 10 and 11 EMIR, or which may have done so only in relation to certain counterparty types or certain product types. However, Article 13 EMIR did not originally envisage that the Commission might grant conditional equivalence decisions. This means that where other provisions cross-refer to Article 13 equivalence decisions it can be unclear how they should be applied. For example, Article 382(4)(a) CRR provides that intragroup transactions "as provided for in Article 3 [EMIR]" should be exempt from CVA but does not provide guidance on how to apply this exemption in the event that an equivalence decision is only granted subject to conditions.

## 2. Comments on the Proposed Equivalence Decision for the US Prudential Regulators[2]

The Proposed Equivalence Decision for the US Prudential Regulators only applies if one of the counterparties is "established" in the US and considered a Covered Swap Entity. This raises the issues addressed below.

**1) Established.** As mentioned in our general comments above, the margin rules (the "**Pru Rules**") imposed by the US Prudential Regulators may apply in circumstances where neither party is established in the US. For example, the margin obligation may apply to a party that is guaranteed by a US entity or (for a party that is a registered swap dealer) to a party that is a non-US subsidiary of a US entity. This means that the Pru Rules would apply in relation to a transaction entered into between an EU subsidiary of a US entity (where the EU subsidiary is

[2] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12865-Financial-market-regulation-EU-recognition-of-US-Prudential-Regulators-rules-on-OTC-derivatives

registered as a swap dealer) and another EU counterparty, but the Proposed Equivalence Decision would not apply to that transaction.

We would welcome confirmation from the Commission that an EU firm may rely on the exemption in Article 13 (and on other exemptions which cross-refer to the equivalence decision under Article 13) where at least one counterparty is subject to the rules of the relevant third country even if neither counterparty is "established" in that third country.

**2) Covered Swap Entities.** The second issue raised by the Proposed Equivalence Decision is that the rule is limited to US counterparties that are Covered Swap Entities. Covered Swap Entities are defined under the Pru Rules as swap dealers (whether in the US or not) registered with the CFTC that are subject to the prudential regulators' margin regulation ("**Dealers**")[3]. However, under the Pru Rules, US counterparties that are not swap dealers (other than corporate end-users) are also subject to the Pru Rules if they face a Dealer. So, for example, a US fund that enters into a swap with a Dealer will be subject to the Pru Rules.

The effect of limiting the equivalence decision to Covered Swap Entities therefore undermines the usefulness of the equivalence decision, narrows the scope of its application, creates an asymmetric application of the rules that serves no policy purpose and introduces a different treatment depending on whether the relevant Dealer is an EU or a US entity. For an EU Dealer, no trade with a US counterparty will benefit from the equivalence decision unless the US counterparty is itself a Dealer. By contrast, for a US Dealer, any trade with an EU counterparty (other than a corporate end-user) will benefit from the equivalence decision. We see no rationale for this distinction. In addition, this issue is becoming increasingly relevant as we move towards phases 5 and 6 of initial margin implementation (which are due to go live in September 2021 and September 2022 respectively), because more and more non-Dealers will be required to post initial margin.

We therefore suggest amending the text of the Regulation as follows:

*…where at least one of the counterparties to those transactions is established in the USA and where at least one counterparty is considered a Covered Swap Entity by [the prudential regulators] and that the Covered Swap Entity counterparty is subject to the Swap Margin Rule laid down in Title 12 of the Code of Federal Regulations…*

## 3. Comments on the Proposed Equivalence Decision for Australia[4]

The Proposed Equivalence Decision for Australia provides that recognition of equivalence should be conditional on the exchange of variation margin between counterparties subject to Article 11 of EMIR and APRA covered entities. We understand that this is because the obligation to exchange variation margin under Prudential Standard CPS 226 only applies to counterparties to a transaction where the amount of non-centrally cleared derivatives of both counterparties exceeds, on an aggregated and consolidated basis, a de minimis threshold of

---

[3] Although the definition of "covered swap entities" also includes registered security-based swap dealers, major swap participants, and major security-based swap participants, no such entities currently exist.

[4] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12863-Financial-market-regulation-EU-recognition-of-Australia-s-rules-on-OTC-derivatives

AUD 3 billion. No such threshold exists under EMIR. However, making equivalence conditional on exchange of variation margin between the counterparties will have a number of potentially adverse consequences, including:

- The exemptions under Articles 11 and 13 EMIR for transactions with a counterparty in an equivalent jurisdiction would not be available in relation to variation margin, even where an APRA covered entity would be required to exchange variation margin under Prudential Standard CPS 226 (and so would in fact be subject to equivalent obligations to those under EMIR).
- The Proposed Equivalence Decision indicates that the parties would need to provide variation margin in all circumstances in order to rely on the equivalence decision. There is no provision made in the Proposed Equivalence Decision for circumstances in which the parties are not required to provide variation margin under EMIR (for example, in relation to physically settled FX forwards and swaps). We would welcome confirmation from the Commission that it is not necessary for the parties to exchange variation margin in circumstances where this is not required under EMIR, in order for the parties to be able to rely on the equivalence decision.
- We would also welcome confirmation from the Commission that firms may rely on the intragroup exemption from CVA under CRR when dealing with counterparties that are APRA covered entities in reliance on this equivalence decision, and that they are not required to monitor individual trades to determine whether or not variation margin has been provided on any given day and whether the CVA exemption applies to each individual transaction as a result.

## 4. Comments on the Proposed Equivalence Decision for Brazil[5]

We note that the Proposed Equivalence Decision for Brazil does not cover physically settled commodity derivatives (other than gold derivatives).

This raises a similar point to the one made above in relation to Australia with respect to reliance on the intragroup exemption from CVA. We would welcome confirmation that firms may rely on the Proposed Equivalence Decision to enable them to apply the intragroup exemption from CVA under CRR where the other criteria are met, and that they are not required to exclude physically settled commodity derivatives from the intragroup exemption.

---

5 https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12860-Financial-market-regulation-EU-recognition-of-Brazil-s-rules-on-OTC-derivatives

## 5. Comments on the Proposed Equivalence Decision for Canada[6]

We note that the Proposed Equivalence Decision for Canada does not cover physically settled commodity derivatives. This raises similar issues to those discussed above in relation to Australia and Brazil.

In addition, we note that the Proposed Equivalence Decision is conditional on the following two conditions being satisfied:

- At least one of the counterparties must be established in Canada and be subject to the margin requirements of Canada;
- Transactions must be marked to market and variation margin exchanged on the same day on which it is calculated (or else the parties agree that variation margin shall be provided within two business days of its calculation and the MPOR used to calculate initial margin is adjusted accordingly).

The requirement for at least one of the counterparties to be established in Canada appears to duplicate the provisions of Article 13(3) EMIR. In any event, as mentioned above, we would welcome confirmation from the Commission that the Proposed Equivalence Decision would apply where at least one counterparty is subject to the margin requirements of Canada (rather than where they are "established" in Canada) as not all entities that are subject to the margin requirements of Canada will be established in Canada.

We would also raise similar comments to those mentioned above in relation to Australia, with respect to the Commission's intention to make this equivalence decision conditional on exchange of variation margin and on marking transactions to market, including:

- The Proposed Equivalence Decision indicates that the parties would need to mark transactions to market and provide variation margin in all circumstances in order to rely on the equivalence decision. There is no provision made in the Proposed Equivalence Decision for circumstances in which the parties are not required to provide variation margin under EMIR (for example, in relation to physically settled FX forwards and swaps), or circumstances in which the parties may need to mark transactions to model rather than to market. We would welcome confirmation from the Commission that it is not necessary for the parties to exchange variation margin or mark to market in circumstances where this is not required under EMIR, in order for the parties to be able to rely on the equivalence decision.
- We would also welcome confirmation from the Commission that firms may rely on the intragroup exemption from CVA under CRR when dealing with counterparties that are subject to the margin requirements of Canada in reliance on this equivalence decision, and that they are not required to monitor individual trades to determine whether or not a particular transaction has been marked to market or whether variation margin has been

---

6 https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12861-Financial-market-regulation-EU-recognition-of-Canada-s-rules-on-OTC-derivatives

provided on any given day and whether the CVA exemption applies to each individual transaction as a result.

## 6. Comments on the Proposed Equivalence Decision for Hong Kong[7]

We note that the Proposed Equivalence Decision for Hong Kong only addresses the margin requirements of the Hong Kong Monetary Authority (**HKMA**). We would welcome confirmation from the Commission that it also intends to issue a similar equivalence decision in relation to the margin requirements of the Securities & Futures Commission, which are consistent with those of the HKMA.

## 7. Comments on the Proposed Equivalence Decision for Singapore[8]

We note that the Proposed Equivalence Decision is conditional on the following two conditions being satisfied:

- At least one of the counterparties must be established in Singapore and be a MAS Covered Entity;
- Transactions must be marked to market and variation margin exchanged on the same day on which it is calculated (or else the parties agree that variation margin shall be provided within two business days of its calculation and the MPOR used to calculate initial margin is adjusted accordingly).

The requirement for at least one of the counterparties to be established in Singapore appears to duplicate the provisions of Article 13(3) EMIR. In any event, as mentioned above, we would welcome confirmation from the Commission that the Proposed Equivalence Decision would apply where at least one counterparty is a MAS Covered Entity (rather than where they are "established" in Singapore).

We would also raise similar comments to those mentioned above in relation to Australia and Canada, with respect to the Commission's intention to make this equivalence decision conditional on exchange of variation margin and on marking transactions to market, including:

- The Proposed Equivalence Decision indicates that the parties would need to mark transactions to market and provide variation margin in all circumstances in order to rely on the equivalence decision. There is no provision made in the Proposed Equivalence Decision for circumstances in which the parties are not required to provide variation margin under EMIR (for example, in relation to physically settled FX forwards and swaps), or circumstances in which the parties may need to mark transactions to model rather than to market. We would welcome confirmation from the Commission that it is

---

7 https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12864-Financial-market-regulation-EU-recognition-of-Hong-Kong-s-rules-on-OTC-derivatives

8 https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12862-Financial-market-regulation-EU-recognition-of-Singapore-s-rules-on-OTC-derivatives

not necessary for the parties to exchange variation margin or mark to market in circumstances where this is not required under EMIR, in order for the parties to be able to rely on the equivalence decision.

- We would also welcome confirmation from the Commission that firms may rely on the intragroup exemption from CVA under CRR when dealing with counterparties that are subject to the margin requirements of Canada in reliance on this equivalence decision, and that they are not required to monitor individual trades to determine whether or not a particular transaction has been marked to market or whether variation margin has been provided on any given day and whether the CVA exemption applies to each individual transaction as a result.

We would welcome the opportunity to discuss these and any related issues further with you and are also very happy to answer any questions you may have in the meantime.