Time to get compliant with OTC derivatives regulations!

In the aftermath of the financial crisis the G20 set challenging requirements on the trading of over-the-counter derivatives (OTC) in 2009. In 2010 the United States passed the Dodd-Frank Act Title VII and within the European Union, EMIR entered into force in 2012. These measures may have direct and indirect effects on Swiss undertakings and it's well known that they develop extraterritorial effects. Moreover, Switzerland intends to respond to these developments with a so-called Financial Market Infrastructure Act ("FinfraG"), which is expected to become effective in the course of 2015 at the earliest.

In 2014 an assessment might be required in order to continue trading in OTC derivatives

2009 2010 2011 2012 2013 2014 2015

G20 Summit
OTC Regulatory Initiatives

Dodd-Frank Act

- July 2010
  Dodd-Frank Act
- October 2012
  Start implementation Title VII
- February 2014
  Start trading via SEF for certain OTC products
- SEF go live
- Obligations may apply (e.g. SD/MSP, Clearing, Reporting, Risk Management)

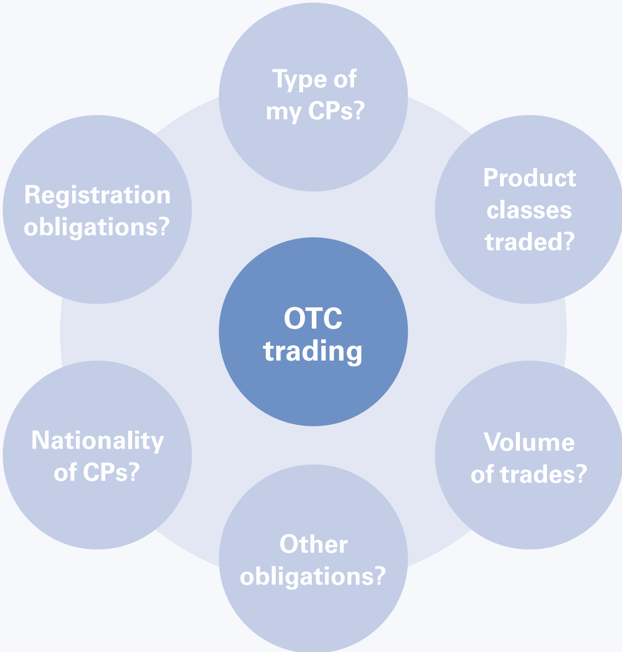
EMIR

- August 2012
  Start EMIR
- February 2014
  Start reporting trades to trade repository
- By end of 2014 start clearing obligation for certain products

FinfraG

- December 2013
  Hearing FinfraG
- FinfraG
  Expected

Impact Assessment – Core Questions



Potential regulatory obligations:
registration, reporting, clearing, risk management, recordkeeping

Swiss undertakings, regulated financial service providers as well as industrial companies should assess their potential exposure to these regulatory requirements:

- Does your company trade in OTC derivatives?
- What are the relevant OTC trades?
- What is the volume of the relevant OTC trades?
- Do your traded volumes potentially lead to registrations requirements e.g. Swap Dealer (SD) or Major Swap Participant (MSP)?
- Which type of counterparties do you use (financial / non-financial entity)?
- Where are your counterparties located (Europe/United States/other country)?
- Could any of your affiliates trigger regulatory obligations?
- Have you been contacted with request for information by any counterparties?
- What needs to be done to be able to continue trading in OTC derivatives?
- What is your organizational setup to assure compliance with OTC products?
- Etc.

Assessment of regulatory setup	Counterparty assessment	Product assessment

OTC regulations under EMIR and DFA

	EMIR	Dodd-Frank Act	Think about impact
Extra-territorial application	– Between EU and non-EU entities and – Potentially between two non-EU entities if there is a direct, substantial and foreseeable effect in the EU	For all swap dealing transactions with US persons (US person definition as proposed by the regulation)	When assessing the counter-parties of OTC trades, the correct application of the relevant definitions is key. You may become subject to regulations even if your direct counterparty is neither located in the EU nor in the US.
Nature counter party	– Financial counterparties – Non-financial counterparties whose positions exceed a certain threshold of trade volume	In general, all participants in swap dealing transactions. However, exemptions may apply (see below exemptions).	No matter whether you are a regulated financial service provider or an industrial company – if you trade in OTC derivatives you may be impacted by the regulation.
Reporting	Both regulatory regimes include the requirement to report derivatives transactions to trade repositories and to keep records of transactions.		Even though you may not be directly responsible for the reporting, the US or EU counterparty will need information from you to fulfill the requirements. However, in certain cases and depending on the nature of the counterparties, non-registered foreign entities may also need to meet the reporting obligation.
Clearing	Central Clearing for certain classes of OTC derivatives	Execution of OTC derivatives subject to the clearing obligation on a swap execution facility (SEF) or designated contract market.	If you want to continue OTC trading, clearing of such derivatives will be a must. It's important to understand what products need to be cleared when and where they are made available for trade.
Risk mitigation	Application of risk mitigation techniques and business conduct requirements	Entity-level as well as transaction-level requirements with regard to business conduct and risk mitigation	You may not directly be required to fulfill any risk mitigation or business conduct requirements. However, in case you get contacted by your counter parties that need your input for their own compliance you should be able to respond adequately.
Record-keeping	Recordkeeping of your OTC trades is one of the most burdensome obligations and constitutes a key principle of OTC regulation. It is a requirement every trading party should attend to in accordance with the respective regulatory frameworks.		
Exemptions	Different exemptions may lower your exposure to the regulation, e.g.: – Thresholds with regard to volume of OTC trades – Product classes (e.g. pure hedge products) – Type of counterparty (e.g. non-financial; registered swap dealer or major swap participant) – Inter-affiliate exemptions for intra-group transactions – Certain participants are exempted from DFA regulation (e.g. commodity pools; private funds; ERISA employee benefit plans; etc.)		

Review current Setup	Design compliant procedures	Value Added
Analysis	Strategy	Risk mitigation & Compliance
– Analyze organizational setup of trading environment – Validate OTC-Counterparties – Analyze OTC derivatives products (transaction validation) – Gap analysis: define areas of deficiency	– Identify different strategic options and their consequences – Modify existing policies and, where needed, create new policies as applicable	– Prevent possible prohibition of certain products – Create value by adapting the portfolio – Prevent regulatory sanctions – Assure compliance in trading transactions

Outlook: FinfraG – Financial Market Infrastructure Act

The planned Financial Market Infrastructure Act contains new regulations regarding authorization requirements and obligations for financial market infrastructures; these include trading venues, central counterparties and central custodians.

Similar to EMIR and DFA, FinfraG will address the clearing of OTC derivative transactions and stipulate respective reporting obligations. FinfraG is expected to come into force in the course of 2015 at the earliest.

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