

MEMO# 32081

December 6, 2019

European Supervisory Authorities Statement on OTC Derivative Contract Fallbacks and Collateral Exchange

[32081]

December 6, 2019 TO: Derivatives Markets Advisory Committee
ICI Global Regulated Funds Committee
ICI Global Trading & Markets Committee
International Compliance Advisory Committee
International Internal Audit Advisory Committee RE: European Supervisory Authorities
Statement on OTC Derivative Contract Fallbacks and Collateral Exchange

On 5 December 2019, the three European Supervisory Authorities (ESAs)[\[1\]](#) published a public statement on the introduction of fallbacks in OTC derivatives contracts and the requirement to exchange collateral.[\[2\]](#)

In the statement, the ESAs acknowledge the interplay between the introduction of fallbacks to increase the robustness of contracts referencing certain benchmarks and the requirement under the European Market Infrastructure Regulation (EMIR) to exchange collateral for certain OTC derivative contracts. The ESAs do not specify in the statement which benchmarks they are referring to, but the statement may be of relevance in the context of the termination of the London Inter-Bank Offered Rate (LIBOR) – currently expected to cease after end-2021[\[3\]](#) – among others.

The statement expresses the ESAs' view that "amendments made to outstanding uncleared OTC derivative contracts ("legacy contracts") for the sole purpose of introducing such fallbacks should not create new obligations on these legacy contracts. In particular, margining requirements should not apply to these legacy contracts where they were not subject to those requirements before the introduction of the fallbacks."

Furthermore, while the ESAs are in contact with European co-legislators concerning possible legislative changes, the ESAs state that they "do not expect competent authorities to prioritise their supervisory actions towards margining requirements (and thus the clearing obligation as well) arising as a result of the introduction of fallbacks in legacy uncleared OTC derivative contracts, and to generally apply their risk-based supervisory powers in their day-to-day enforcement of applicable legislation in this area in a proportionate manner."

Giles Swan
Director of Global Funds Policy, ICI Global

endnotes

[1] The European Banking Authority, the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority

[2] https://www.esma.europa.eu/sites/default/files/library/esas_2019_19_statement_on_the_introduction_of_fallbacks_in_otc_derivative_contracts_to_increase_contract_robustness.pdf

[3] <https://www.fca.org.uk/markets/libor>

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.