

Meeting Minutes

Financial Markets Law Committee/Financial Markets Lawyers Group
Quarterly Discussion Forum

Thursday, February 14, 2019
10:00 a.m. – 11:00 a.m. (New York time)

Financial Markets Law Committee (“FMLC”): Carolyn Jackson, Venessa Parekh, Joanna Perkins

Financial Markets Lawyers Group (“FMLG”): James Brown, David Buchalter, Chinedu Ezetah, Terence Filewych, Jill Hurwitz, Glade Jacobsen, Robert Klein, Nancy Rigby, Lisa Shemie, James Wallin, Frank Weigand

Federal Reserve Bank of New York (“FRBNY”): Raymond Check, Thomas Noone, Janine Tramontana, Shawei Wang

Additional participants: Amelia Kaufman (Deutsche Bank), Olivia Wang (Morgan Stanley)

The meeting was conducted telephonically.

Brexit update

FMLC Chief Executive Joanna Perkins opened the call with a recap of recent political and legal developments concerning Brexit. She reported that, in both respects, little progress had been made since the previous quarterly call. In January, the Prime Minister’s proposed withdrawal agreement failed to pass the House of Commons, and by an historic measure. After surviving a vote of no confidence tabled by the opposition party, the government began new and, so far, unfruitful negotiations with the remaining 27 member states of the EU. The so-called “Irish backstop”—a negotiated fallback provision that would create a regulatory border between Northern Ireland and the rest of the UK as an alternative to border checks along the Irish border—remains the most contentious issue.

Dr. Perkins presented briefly four possible outcomes: (1) a “no deal” Brexit ; (2) an amended version of the current draft “deal” is accepted; (3) a general election or second referendum which has been deemed by the Government not possible before March 29, 2019—“exit day;” and (4) an extension of the Article 50 notice period which would push back “exit

day.” Dr Perkins stated that it was not possible to predict which outcome would prevail but observed that the markets had expressed support for an extension. The FMLC has focused its efforts on reviewing and commenting on draft legislation for incorporating EU regulation into UK law. Asked whether European regulators would recognize rates offered by UK-based benchmark administrators, Dr. Perkins shared a general market expectation that major UK benchmarks would be approved for use in the EU.

LIBOR transition

Dr. Perkins provided an overview of two strands of work on critical international benchmark rates: (1) improving unsecured bank funding (“IBOR”) benchmarks through more reliable input data, and (2) replacing IBOR benchmarks with “risk free rates” (“RFRs”) that rely on central bank overnight borrowing data—SONIA, SOFR, TONAR, and SARON being examples from the Bank of England, Federal Reserve, Bank of Japan, and Swiss National Bank, respectively. Addressing the first strand, Dr. Perkins noted that ICE Benchmark Administrator (“IBA) expects to continue providing LIBOR through 2021. To continue LIBOR beyond that, IBA announced reforms that decrease the reliance on dealer polls. Even so, the general consensus is that LIBOR cannot be sustained for currencies other than the U.S. dollar and, possibly, GB Sterling. Moreover, the Financial Conduct Authority’s Chief Executive, Andrew Bailey, has sent strong signals encouraging firms to use RFRs in new contracts and to amend existing contracts to replace IBORs with RFRs. The discussion that followed addressed, among other issues, the risks and benefits resulting from different methodologies used in the various RFR rates, the continuity of contracts if the IBORs—LIBOR especially—are discontinued without fallback rate provisions, the suitability of term rates versus overnights for certain segments of the market, and the coordination among central bank-sponsored working groups that have produced RFRs for major currencies.

Overlapping global standards

FMLG Secretary Thomas Noone summarized recent FMLG discussions about overlap between standards and best practices published by the FICC Market Standards Board (“FMSB”) and the FX Global Code. These discussions have addressed two related but distinct scenarios. The first arises when FMSB standards and the FX Global Code overlap but do not conflict. Some members of the FMLG have cautioned that the Code was intended to be the sole authority on foreign exchange practices to the exclusion of all others. The second scenario involves an actual conflict between two authorities, which prompts questions about which takes precedence. Mr. Noone observed that he is not aware of any actual conflicts between FMSB publications and the FX Global Code. There is, however, some conflict between one of the FMSB’s transparency drafts and the best practices published by the Treasury Market Practices Group, a committee sponsored by the FRBNY. Mr. Noone suggested further discussion about overlapping global standards at this year’s Quadrilateral meeting.

EU benchmarks regulation

Mr. Noone reported that for several months the FMLG has discussed the application of EU benchmark regulations to the leading rate sources for eight or nine currencies including the Korean won, the Taiwanese dollar, and the Philippine peso. These rate sources are published by a local administrators that, to date, have not received approval from EU regulators, which is required in order to be used in currency contracts involving covered EU counterparties after January 2020. FMLG members are concerned that the lack of approval before the regulatory deadline could lead to a market fragmentation in non-deliverable forward contracts that incorporate those rates. Several trade associations have advocated for legislative relief in the form of a two-year extension of the approval deadline for third-country and other benchmarks.

U.S. regulatory update

Chinedu Ezetah addressed revisions proposed by the U.S. Commodity Futures Trading Commission (“CFTC”) to its rules governing swap execution facilities (“SEFs”). Among other changes, the CFTC proposes more flexibility for SEFs to determine what trading functionality and execution methods they want to offer. The revisions also ban certain pre-execution communications, trigger the mandatory trading requirement for a swap that is subject to mandatory clearing upon the mere listing of that swap by a single SEF, codify footnote 88 and expand the scope of entities subject to SEF registration. The general market view is that several aspects of the proposal are favorable, while some aspects either create new challenges or potentially exacerbate existing challenges with the current SEF rules that has led to a fragmentation of liquidity. Several industry groups are preparing comment letters, with the deadline for commentary extended to March 15th.

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