

**International Swaps and Derivatives Association
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**CEO's Remarks – Leading the Market
Scott O'Malia
8.45am April 13, 2016**

Good morning, everyone. A very warm welcome to our 31st International Swaps and Derivatives Association (ISDA) annual general meeting (AGM) here in Tokyo. It's a genuine pleasure to be back again for our flagship event – and we've just about timed it perfectly for the cherry-blossom season.

I first came to Japan 30 years ago as a student. This was also coincidentally ISDA's first year of operation. I spent as much time as I could learning about Japan – and I learned I have absolutely no talent whatsoever when it comes to karaoke. I remember that while I was here, I managed to pick up what was then considered to be cutting-edge technology – a Sony Walkman.

Technology has changed in so many ways since then – and I will address this in more detail later. But, in the time since I was here as a student, ISDA has also gone from strength to strength.

ISDA has now established a 30-year track record of success, and is doing more each and every day to lead the market through advocacy for safe, efficient markets. We've led development of legal standards, and have expanded our expertise to represent the evolving derivatives market structure, including data reporting, clearing and trading.

I don't need to remind this crowd that a lot of effort has been put into meeting the Group-of-20 (G-20) derivatives reforms over the past six years. To ease that transition, ISDA has been there to develop solutions, advocate for coherent and consistent rules, and highlight the impact of the capital rules with solid quantitative analysis. I am proud of the work we have done – and there is plenty more to do.

Today, I'd like to cover three topics to give you some perspective on ISDA's important work and how we will be leading the market into the future.

First, I'd like to highlight what we have achieved, and how we are evolving with the new market structure.

Next, I'll share with you some of our current priorities.

Finally, I'd like to sketch out where ISDA is headed.

Delivering Results

In many respects, the AGM this year comes at a bit of an inflexion point for the derivatives market. This September will mark the rollout of the last big plank of the G-20 derivatives reform commitments, as new margining rules for non-cleared derivatives are phased in.

Let's start with a reminder of what ISDA has achieved recently, and why it is so vital to this market.

Thirty years ago, this organization was founded with a goal of developing a Master Agreement to standardize and simplify the trading of derivatives.

That strong legal foundation remains in place today, and is unmatched by any other association. We now have over 850 members in 67 countries – and we're continuing to grow. We are a genuinely global association with 105 staff located in six countries, dedicated to serving our membership and pushing for consistent rules around the world.

While we are well known for the ISDA Master Agreement – particularly since our mention by Brad Pitt in the Big Short – our collateral documentation, and our collateral and netting opinions are also highly valued by members.

Last year saw the publication of the first clean netting opinion in Malaysia, and the first Middle Eastern netting opinion in UAE. A lot of resource is dedicated to maintaining those opinions – for instance, we annually update over 100 netting and collateral opinions in Europe alone.

Last year also saw the relaunch of the ISDA Resolution Stay Protocol to cover securities financing transactions. That protocol – signed by 21 global banks at launch – opts adhering parties into certain special resolution regimes to ensure a consistent cross-border approach in the event a bank enters into resolution. We're currently looking at other resolution regimes beyond the initial six identified by the protocol.

ISDA is also working with buy-side members to launch a separate Jurisdictional Modular Protocol, which will enable firms to comply with national regulations. That protocol will be ready shortly, and will include the necessary flexibility the buy side has requested.

Data and Reporting

I'd like to flag another example – data and reporting. This is an area where ISDA has been leading the market. That includes establishing Financial products Mark-up Language (FpML), which has become an essential tool in defining derivatives trades and provides a consistent taxonomy for the entire market.

Building on our long-time data expertise, ISDA has been hard at work developing real solutions to the global data reporting puzzle. We have been at the forefront of advocating for global harmonization by leading a global coalition of derivatives users. Over the past year, ISDA has been called upon twice to testify before Congress to urge a more coherent reporting standard, as well as submitting hundreds of pages of comment letters on this topic.

ISDA has also published key principles papers on data harmonization – with our most recent published today. This paper urges regulators to recognize that the reporting responsibility should rest solely with a single party, rather than requiring both counterparties to report the same data.

We believe this change will increase consistency and accuracy of the data that is reported, as well as relieving end users of an unnecessary reporting burden. This paper was co-authored with a dozen end-user and buy-side groups.

The lack of globally consistent rules, and the use of different reporting formats and data fields, has meant regulators are unable to aggregate exposures and spot possible systemic risks – a key objective of the G-20 derivatives reforms. In response, the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions (CPMI-IOSCO) have launched a data harmonization project to agree consistent standards for unique transaction identifiers (UTIs), unique product identifiers (UPI) and other data elements.

ISDA wholeheartedly supports this project, and has advocated for national regulators to delay rolling out their own requirements until CPMI-IOSCO completes its important work. We've also established an industry-wide Symbology initiative to help create a globally consistent product identifier to represent all trades consistently throughout the trade lifecycle.

Capital

I'd also like to touch upon capital. We know this is an important topic for our members, and ISDA has now made this a key strategic priority. We've also delivered results.

In the past 12 months alone, ISDA has coordinated broad industry impact studies on the Fundamental Review of the Trading Book (FRTB), the review of the credit valuation adjustment (CVA) capital charge and the net stable funding ratio.

Other initiatives include an assessment of the leverage ratio. Here, we have challenged the failure to recognize the exposure-reducing effect of client cash collateral within the Basel framework. We believe client initial margin reduces risk, and should be reflected in capital charges. The capital rules must properly align with the risk-reducing behavior of clearing, not punish it.

I am extremely proud of the work conducted by our capital team to crunch the data supplied by our members to specifically and accurately highlight the impact of the capital rules.

We're currently leading another industry initiative to assess the impact of the final FRTB rules, and we will share some of those results with you at the specialist FRTB panel tomorrow afternoon.

This work is vital. ISDA supports an appropriate, consistent and risk-sensitive capital framework. It's therefore important the impact is fully understood, both on individual bank business lines and end users. ISDA's work is an important contribution to that. Where the impact is found to be greater than expected, regulators should look to make the necessary recalibrations and adjustments to avoid overly negative effects.

To be clear, we're not asking for any part of the Basel III framework to be reversed. Only that the calibrations are appropriate. In this regard, we welcome a recent statement from the G-20 supporting further work to refine the Basel III framework to ensure its coherence, but without significantly increasing overall capital requirements.

We need to make sure the capital framework properly balances safety and soundness, while at the same time enabling growth, lending and investment.

Current Priorities – Leading the Market

As you can see, ISDA has played a leading role in establishing a sound legal framework, advocating for globally harmonized data rules, and pushing for consistent and reasonable capital requirements.

I'd now like to turn to our current activities, and share with you how ISDA is evolving to adapt to the new market conditions driven by regulation.

As you know, ISDA represents the entire derivatives industry, whether exchange-traded, cleared or bilateral. As such, we thought it was important to update our mission statement and strategic priorities to reflect this.

One of the things we won't be changing is our commitment to safe and efficient markets.

That means we'll be retaining our strength in developing the technical solutions, the market standards and the legal documentation that our members need to run their businesses.

But the derivatives markets today are clearly very different to the derivatives markets before the financial crisis. Trade reporting is now the norm. Clearing is increasingly common, and electronic execution is gaining momentum. There are a host of new infrastructures that must be integrated into the lifecycle of a trade, and there are now more links in the chain between buyer and seller.

In short, the changes in market structure driven by regulations have been profound, and the evolution is still ongoing. In response, ISDA is providing solutions to harmonize the global rules and to help achieve cost-efficiency.

This was the rationale for the changes to our mission and strategy statement earlier this year. The motivation was simple: we wanted to ensure our strategic priorities continue to mirror this evolving market structure and reflect the main concerns of our diverse membership.

Among the changes is an explicit commitment to enhance ISDA's attention on derivatives trading and reporting practices, which will sit alongside an emphasis on clearing to ensure ISDA retains a strong focus on safe, efficient market infrastructures.

The mission statement also includes an explicit pledge to ensure a prudent and consistent regulatory capital and margin framework.

Margin for Non-cleared Derivatives

Our work on the new margin rules has been under way for the past three years and is truly market changing – similar to the role ISDA played when it created the first Master Agreement for bilateral trades. The effort will deliver a comprehensive margining solution, which includes a consistent margin methodology, a transparent governance framework, and the necessary legal documentation.

The various strands of this initiative are now close to fruition. Now that US, European and Japanese regulators have published their requirements, the final push to implementation can begin.

A central part of this project is the development of a standard initial margin model, known as the ISDA SIMM, which will be available for firms to use to calculate how much initial margin needs to be exchanged.

The model is now finished from a design perspective. ISDA has been touring the globe in recent months, showing the methodology to regulators, alongside a transparent governance structure, in order to smooth the path to implementation.

We're now at the stage of licensing the model to users, and our revised licensing program was published this month. For those who are interested, the methodology is published on our website.

Another big focus has been preparing for the necessary revisions to ISDA credit support documentation in each jurisdiction. Again, we're making very good progress here, and the first margin-compliant documents will be published in the coming days.

ISDA is also developing a protocol to ensure the changes can be made to outstanding agreements as efficiently as possible.

There's still a lot that still needs to be done. But ISDA is working hard to deliver solutions in advance of the regulatory mandates.

We have a panel dedicated to this topic tomorrow, so please come and listen to get a full update on where we are with this project.

Clearing

Another topic that features prominently in our mission statement is clearing. Much of our work here is focused on making sure clearing can work effectively, building on our legal and documentation expertise. That includes our clearing opinions, and our series of classification letters.

As clearing volumes have grown and new clearing mandates have come into force, ISDA has provided research and analysis on central counterparty (CCP) resilience, and proposed a framework for CCP recovery.

Attention is now turning to the important issue of CCP resolution, and ISDA has been very active in contributing ideas to this debate. Among the key issues is understanding how resolution and recovery differ in terms of tools, resources and powers, and grasping where recovery ends and resolution begins.

Our CCP recovery and resolution panel this afternoon will give you a flavor of some of the important questions being debated.

Trade Execution

Turning to trade execution. The G-20 reforms have made price discovery and trade execution a key regulatory objective. And ISDA is bringing a multifaceted approach to providing industry solutions on trade execution. Marrying technical legal expertise and operational know-how, ISDA is developing solutions to provide consistency and clarity on trade-execution rules.

For example, we recently published a paper that sets out a detailed comparison of similarities between US and European trading-platform rules to help facilitate substituted compliance decisions.

Learning from the mistakes that contributed to the three-year deadlock on CCP equivalency, ISDA has developed a legal roadmap to establish the basis for a finding on comparability between US and EU rules. Our detailed report finds that both sets of rules deliver the same outcomes on trade execution. Going forward, we want to see market participants making trading decisions based on price and size, not based on regulatory factors.

On the operations side, I'm pleased to report that ISDA brokered a regulatory solution to define straight-through processing (STP). The consensus solution between our members and regulators was for the affirmation of swap execution facility (SEF) trades within 10 minutes of execution.

MIFID II

In Europe, ISDA has also employed its research arm to conduct detailed analysis on European trading volumes as part of the revised Markets in Financial Instruments Directive (MIFID II) consultation process. In particular, our work on Europe's size-specific-to-the-instrument (SSTI) thresholds, and our finding that proposed pre-trade SSTI levels should be reduced, has been adopted in European Commission (EC) recommendations. This is a victory for our membership and validation that our fact-based advocacy strategy pays off.

We've got a tremendous amount of work to do with MIFID II, and so much of that is contingent on different elements being in place for the entire package to work. This would have been challenging under the original schedule, so we are grateful for the agreement by European legislators and policy-makers to delay implementation.

We won't take a break during this period, but will work with our members to develop policy and operational solutions to help implement the requirements in 2018.

Our specialist MIFID II panel tomorrow afternoon will tackle these important issues and provide an update on the work ISDA is doing.

Looking to the Future

I've talked about both our long-standing capabilities and how we have successfully responded to the regulatory changes in the market. So let me turn to the future and share with you where ISDA is headed.

The changes I've described are resulting in an evolution in the universe of firms that participate in this market. Some established players are rethinking their business mix. Other new entrants are stepping in, focusing on niche areas of interest. A whole new ecosystem of fintech providers is also springing up, hoping to tap into a desire to outsource collateral management and valuation services.

To prepare for this shift, and to better focus on the opportunities for setting operational standards, ISDA has reorganized its Market Infrastructure and Technology policy team to explicitly target this space. This will be an important area for us. Standardization facilitates greater automation and cost-efficiency, and ultimately frees up resources to focus on innovation.

Recall that when I first arrived in Japan 30 years ago, I wanted the best-in-class technology – a thin Sony Walkman to play my favorite cassettes. Today, technology has advanced and continues to progress, and provides unbelievable opportunities. At ISDA, we are working to help our members adapt and harness technology to cut costs and improve services.

The Market Infrastructure and Technology Policy Team has already restructured ISDA's infrastructure working groups to better identify and focus on market sectors that are ripe for standardization and innovation. As part of this, we have spotted a couple of areas where we think we can help the market.

The first is collateral management. Building on the changes we are implementing through our work on the non-cleared margin reforms, we see a huge opportunity for optimization of collateral management. We will continue to engage with our members to find cost savings through automation in this sector.

Another is the often-talked-about block chain. This technology has dominated the fintech discussion recently, and appears to offer terrific opportunities for innovation and cost savings.

ISDA is exploring these opportunities too. What we know is that block chain will not succeed without standards – and this is something ISDA is very good at. We also want to ensure FpML and the huge number of contracts ISDA has developed can be used as the basis for 'smart contracts', which essentially allow self-performing transactions, enabling them to benefit from block-chain technology.

As I noted earlier, the market structure is evolving. These changes are bringing in a variety of new participants, and are likely to result in a change in the dynamics of derivatives markets.

In response, the ISDA Board has voted to broaden its scope and perspective by appointing members from diverse sections of the market. The aim is simple: to make sure the composition of the Board reflects ISDA's already diverse membership, and ensure we have broader expertise to help shape our priorities going forward.

We'll be making announcements on the new Board members in the coming weeks and months.

As we all know, managing costs and resources will be key ingredients to success in the current environment. Greater automation will be vital to achieving that. And standardization is an important pre-cursor for that. That's ISDA's strength.

So, there you have it: the past, the present and the future, all in 20 minutes. This is just a helicopter view of all the hard work that the ISDA staff and you – our members – have been doing to ensure the foundations are in place to maximize the ability of industry participants to thrive in the new market structure.

I am very proud of all we've achieved to develop standards, help solve problems and assist the industry transition to the new regulatory environment.

I am grateful that so many of you have made the trip to join us here in Tokyo – which, for the next two days – will be the center of the derivatives world. You can look forward to in-depth debate of critical issues during our panel discussions. You'll have the opportunity to connect with old friends and colleagues. Most importantly, I hope you enjoy the next two days in Tokyo.

Thank you so much for coming – Enjoy the AGM.

Thank you.