

WRITTEN TESTIMONY OF CHRIS EDMONDS,
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ON BEHALF OF INTERCONTINENTAL EXCHANGE, INC.
BEFORE THE HOUSE AGRICULTURAL SUBCOMMITTEE ON COMMODITY EXCHANGES,
ENERGY AND CREDIT

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Introduction

Chairman Scott, Ranking Member Scott, I am Chris Edmonds, Senior Vice President, Financial Markets for Intercontinental Exchange, or ICE. I appreciate the opportunity to appear before you today, as this Committee looks at Brexit, the European Commission's recent reforms to its legislation governing the regulation and supervision of CCPs, called the European Market Infrastructure Regulation (or EMIR 2.2), and related cross-border issues.

Central counterparties (or CCPs) play a critical role in the financial markets that serve the needs of market participants around the globe. Policy makers across the world, including this Committee, have an interest in safe and efficient markets. To further the common interest of well-functioning markets and well-regulated CCPs, we appreciate the opportunity to participate in this hearing as it examines the cross-border supervision of CCPs.

Background

Since launching an electronic over-the-counter (OTC) energy marketplace in 2000 in Atlanta, Georgia, ICE has expanded both in the U.S. and internationally. Over the past seventeen years, we have acquired or founded derivatives exchanges and clearing houses in the U.S., Europe, Singapore and Canada. In 2013, ICE acquired the New York Stock Exchange, which added equity and equity options exchanges to our business. Through our global operations, ICE's exchanges and clearing houses are directly regulated by the U.S. Commodity Futures Trading Commission (CFTC), the Securities and Exchange Commission (SEC), the Bank of England, the U.K. Financial Conduct Authority (FCA), the European Securities and Markets Authority (ESMA) and the Monetary Authority of Singapore, among others.

ICE has a successful and innovative history of clearing exchange traded and OTC derivatives across a spectrum of asset classes, including energy, agriculture and financial products. Today, ICE owns and operates six geographically diverse clearing houses that serve global markets and customers across North America, Europe and Asia. Each of these clearing houses is subject to direct oversight by local national regulators, often in close coordination and communication with other regulatory authorities with important interests, and subject to regulations reflective of the G-20 reforms and IOSCO principles.

ICE acquired its first clearing house, ICE Clear U.S., as a part of the 2007 purchase of the New York Board of Trade. ICE Clear U.S. is primarily regulated by the CFTC and is recognized by ESMA and clears a variety of agricultural and financial derivatives. In 2008, ICE launched ICE Clear Europe, the first new clearing house in the UK in over a century. ICE Clear

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Europe clears derivatives in several asset classes, including energy, interest rates, equity and credit derivatives, and is primarily supervised by the Bank of England, in close cooperation with the CFTC, the SEC and ESMA. ICE Clear Credit was established as a trust company in 2009 under the supervision of the Federal Reserve Board and the New York State Banking Department and converted to a derivatives clearing organization (DCO) following implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). ICE Clear Credit is primarily regulated by the CFTC and SEC and also recognized by ESMA and clears a global set of credit default swaps on indices, single names and sovereigns. ICE also operates ICE Clear Netherlands under the regulatory supervision of De Nederlandsche Bank, Autoriteit Financiële Markten and ESMA and ICE Clear Singapore which is overseen by the Monetary Authority of Singapore.

CCPs Vital Role in the Derivatives Market

The risk reducing benefits of central clearing have long been recognized by users of exchange-traded derivatives (futures) and the pre-existing regulatory framework and efficacy of the clearing model throughout even the most challenging financial situations made it the natural foundation of the financial reforms put forward over the past decade. Clearing has consistently proven to be a fundamentally safe and sound process for managing systemic risk. Observers frequently point to non-cleared derivative contracts as a significant factor in the broad reach and complexity of the 2008 financial crisis, while noting the relative stability of cleared markets.

The disciplined and transparent risk management practices of regulated clearing houses serve to reduce systemic risk. A clearing house, by acting as a central counterparty, to clearing members' transactions, eliminates the bilateral counterparty credit risk and imposes on clearing members a transparent set of rules and prudent risk management practices, such as margin requirements, to minimize risks managed by the clearing house. Over the past 100 years, clearing house risk management practices have been repeatedly tested and proven in resolving clearing member defaults including large bankruptcy proceedings, such as Lehman Brothers and MF Global. The recent introduction of mandated clearing obligations for certain swaps has sensibly extended the significant benefits of clearing to a broader array of financial instruments.

Regulatory Cooperation

Following the 2008 financial crisis, global regulators were tasked with implementing the G-20 reforms to achieve the goals of increased financial stability, resilience and transparency in the global OTC derivatives market. Over the last decade, ICE has worked with global regulators as they implement reforms designed to foster financial stability, facilitate robust, liquid and transparent markets, and protect the geographically diverse users of those global markets.

It is well understood by regulators and market participants that the derivatives markets are global markets, as participants in those markets trade across venues and jurisdictions to meet their unique business needs. To realize the goals of the G-20 reforms, it is essential that regulators share information and continue to cooperate with each other, consistent with agreed upon global frameworks. It is important that regulators carefully implement regulatory requirements to minimize the fragmentation of markets and liquidity, which can reduce the

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efficacy of commercial firms' risk management efforts and undermine the goals of financial stability and resilience. To this end, constructive relationships among regulators are critical to building the confidence and trust essential for effective cross-border regulatory frameworks and that are consistent with globally agreed to principles. This effort to work together is in all of our best interests, just as the prevention of market fragmentation should be. Such deference and cooperation can enhance liquid, well-functioning markets and minimize confusion and inefficient, duplicative oversight.

ICE supports the ongoing dialogue between European and U.S. policy makers where there have been notable successes. The 2016 agreement between the European Commission (EC) and the CFTC established a common approach to the regulation and supervision of cross-border CCPs (CCP Agreement).¹ The CCP Agreement promotes regulatory deference as well as prioritizes provisions supporting robust global derivatives markets. In addition, the CFTC, Bank of England and the Financial Conduct Authority recently issued a joint statement providing assurances to market participants on the continuity of derivatives trading and clearing activities between the UK and U.S. regardless of the outcome of the UK's withdrawal process from the EU. Similarly, the EU announced its intention to continue to recognize UK-based clearing firms after the UK's withdrawal process from the EU. Together, these authorities took cooperative measures to avoid regulatory uncertainty about the continuation of the global derivatives market regardless of their location; such an important step achieved through communication, coordination and local regulatory frameworks established based upon global principles. These measures give confidence to market participants about their continued ability to trade and manage their global risks on a cross-border basis.

Continued regulatory cooperation is imperative, as issues such as Brexit, which should have no bearing on these efforts, are determined by other political bodies. ICE has a long history of working with U.S. and global regulators on mutually beneficial supervisory outcomes. Differences and unsubstantiated changes in financial sector reforms can lead to overlapping or conflicting requirements. By working together across the globe, regulators can avoid this harmful and counterproductive outcome and promote a more resilient financial system. This spirit of cooperation should guide our ongoing discussions on critical cross border issues, including EMIR 2.2 implementation and potential Brexit responses.

EMIR 2.2

Recently, the European Parliament and EU-Member States reached an agreement on reforms to EMIR 2.2, legislation governing the regulation and supervision of CCPs. Prior to this announcement, the EU's approach to supervising non-EU CCPs was based on equivalence and deference to the 2016 CCP Agreement. EMIR 2.2 expands the regulatory and supervisory authority of ESMA over third-country CCPs, i.e., non-EU domiciled CCPs, if those CCPs are determined to be systemically important for the financial stability of the EU. EMIR 2.2 contemplates that, with respect to non-EU domiciled CCPs determined to be systemically important, ESMA could rely on comparable compliance with the CCP's local regulatory regime. EMIR 2.2 also contemplates that ESMA be able to recommend, and the Commission be able to

¹ Joint Statement from CFTC Chairman Timothy Massad and European Commissioner Jonathan Hill, CFTC and the European Commission: Common approach for transatlantic CCPs (February 10, 2016), <https://www.cftc.gov/PressRoom/PressReleases/pr7342-16>.

adopt, after agreement from the ECB, an act that requires a clearing house to relocate to the EU if the CCP or some of its clearing services are deemed to be of such systemic importance. We agree with the final agreement of the European Parliament and Council that such an act should be a measure of last resort, as such a requirement would increase costs considerably for banks and their customers, because the current portfolio efficiencies would be unavailable if the euro-denominated portion were disaggregated. A better outcome would be to continue the development and reliance on a model of supervisory cooperation that enables EU supervisors to exercise appropriate and proportionate oversight of CCPs that provide clearing services in the EU.

ESMA recently published two consultations on the implementation of the new EMIR 2.2 regime for non-EU domiciled CCPs. Specifically, ESMA is currently seeking public consultation on the criteria for assessing the systemic importance of non-EU domiciled CCPs. ESMA is also consulting on the detailed rules regarding ESMA's approach to comparable compliance. ICE is evaluating ESMA's recently published consultations and will be commenting. ICE supports the EMIR 2.2 goal to establish appropriate supervision of non-EU domiciled CCPs that are determined to be systemically important for the financial stability of the EU and looks forward to contributing to the dialogue on implementation of EMIR 2.2.

The European Commission's policy goals to ensure appropriate supervision of non-EU domiciled CCPs that are deemed systemically important to the EU are understandable. ICE believes that these goals can be achieved by ESMA employing mechanisms based on international standards such as CPMI-IOSCO, together with continued cooperation and information-sharing agreements among CCP supervisory authorities. These mechanisms can provide ESMA with the information and oversight they require, while leaving the final decision-making in the hands of national regulators to prevent overlapping or conflicting requirements, which is particularly critical in a time of crisis. ESMA, in any effort to enhance oversight of non-EU CCPs, should consider strong and effective supervisory cooperation between the relevant authorities. This approach will enable EU supervisors to exercise appropriate and proportionate oversight of non-EU CCPs.

A global approach to supervision brings significant benefits. Especially in a crisis situation, the market needs clarity that the national regulator can take the lead in managing a default and have the ultimate decision making authority. The national regulator should consider the interests of other relevant authorities and interested parties when managing a crisis, however there should be no ambiguity in the ultimate decision making authority.

CFTC Cross-Border Regulation

In 2018, the CFTC indicated its desire to reassess the current cross-border application of its swaps regime with a rule-based framework based on regulatory deference to third-country regulatory jurisdictions that have adopted the G-20 swaps reforms.² The CFTC has stated that, as global regulators continue to implement swaps reforms in their markets, it is critical to ensure CFTC rules do not conflict and fragment the global marketplace. The CFTC has proposed to

² "Chairman Giancarlo Releases Cross-Border White Paper", October 1, 2018 at: <https://www.cftc.gov/PressRoom/PressReleases/7817-18>.

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move to a flexible, outcomes-based approach for cross-border equivalence and substituted compliance and to employ deference to overseas regulators. To this end, Chairman Giancarlo has recently described a new approach to supervising certain foreign derivatives clearing organizations (DCOs). This approach would introduce an alternative compliance regulatory framework for those foreign DCOs that do not pose a substantial risk to the U.S. financial system and would rely on the DCOs' home country rules to a large extent. ICE supports this type of approach and hopes the CFTC will publish the proposal for comment shortly.

ICE believes that the cross-border oversight and regulatory deference to home country regulators is essential to well-functioning markets. The CFTC's recent publications and Chairman Giancarlo's description of his vision for future CFTC rule proposals are, in ICE's view, positive steps towards implementing relevant laws, standards, and policies that further the goal of financial stability and resilience, while minimizing supervisory duplication and conflict.

Conclusion

ICE has always been, and remains, a strong proponent of open and competitive markets with appropriate regulatory oversight. As an operator of global futures and derivatives markets, ICE understands the importance of ensuring the utmost confidence in its markets and we take seriously our obligations to mitigate systemic risk. To that end, we have worked closely with regulatory authorities in the U.S. and abroad in order to ensure they have access to all relevant information available to ICE regarding trade execution and clearing activity on our markets. We look forward to continuing to work closely with governments and regulators at home and abroad to address the evolving regulatory challenges presented by derivatives markets and to expand the use of demonstrably beneficial clearing services that underpin the best and safest marketplaces possible.

Mr. Chairman, thank you for the opportunity to share our views with you. I would be happy to answer any questions you and members of the Subcommittee may have.