European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

EACB Response to the Public consultation on Regulation (EU) no 648/2012 on OTC derivatives, central counterparties and trade repositories

12 August 2015

The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 31 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4,200 locally operating banks and 68,000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 205 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 78 million members and 860,000 employees and have a total average market share of about 20%.

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Introduction

The European Association of Co-operative Banks (EACB) welcomes the opportunity to contribute to the discussion around the review of EMIR. Bearing in mind the revolution that EMIR has caused to the derivatives markets and that it is one of the first regulations with a massive amount of delegated regulations drafted by ESMA (or other European supervisory authorities) we believe that a more in-depth analysis of EMIR and its implications is indeed a timely exercise.

One of the biggest problems for our smaller members is the difficulty in accessing CCPs, while other requirements have proven to be too costly and burdensome. We believe that more simple procedures could be envisaged.

Executive summary

- The EACB supports the exclusion from EMIR central clearing and margin requirements of all non- systemically important firms – that is also smaller Financial Counterparties (FC) and not just the Non Financial Counterparties (NFC). Indeed, small and medium-sized FCs have severe problems to enter into clearing relationship, due to both cost and availability issues. Indirect or client clearing offerings have not proven to be successful due to legal and practical challenges. Therefore a small number of clearing members are able to offer to clear on behalf of smaller counterparties but at a cost totally disproportionate compared to the business of smaller players.

Should no solutions become available, small banks, building societies and financial firms will de facto not be able to keep an efficient risk management activity (particularly for the interest rate risk) by means of trading OTC derivatives to hedge their positions. This hedging is a vital part of the retail and real economy focused business of cooperative banks, providing an essential managing tool that then allows those banks to effectively finance individuals and SMEs. Due to these problems, the clearing obligation is unintentionally forcing smaller financial firms out of the derivatives markets. This reduces competition and shifts market balance. Pushing these companies out of business would deteriorate the credit conditions of SME segment even further and thus jeopardize the fragile recovery of European economies. This would be inconsistent with the Capital Market Union policy agenda aiming to remove barriers to the free flow of capital in Europe and the variety of other policy makers' positive initiatives to stimulate economic growth in Europe.

- In that regard, the EACB also draws to the Commission's attention that the current EU regime under EMIR is far more burdensome for small banks than in other major jurisdictions. The principal example, of course, is the US, where the equivalent central clearing regime introduced under the Dodd Frank Act.
- Client clearing exposure should be held outside the Basel III leverage ratio rules and the initial margin requirements should be excluded from the rules as well. This would ensure for an equitable balance between the cleared world and the bilateral world.
- A public database/register collecting all relevant information and accessible to all parties would create transparency, consistency and legal certainty for all parties.

- The frontloading requirements for category 1 and category 2 parties (expected to be the rule in the RTS) will lead to legal uncertainties, inconsistencies, pricing issues and monitoring/operational issues (IT setup, etc.).
- The EACB is supportive of an internationally consistent definition of non-financial counterparties (NFC) (i.e. non-systematically important counterparties.)

Please find our detailed responses to the consultation below.

Responses to the Consultation Questions

PART 1

Question 1.1: CCP Liquidity

Article 85(1)(a) states that: "The Commission shall …… assess, in cooperation with the members of the ESCB, the need for any measure to facilitate the access of CCPs to central bank liquidity facilities."

There are no provisions under EMIR facilitating the access of CCPs authorised under EMIR to additional liquidity from central banks in stress or crisis situations, either from the perspective of the members of the ESCB or from the perspective of CCPs. However, it is recognised that in some member states, CCPs are required to obtain authorisation as credit institutions in accordance with Article 6 of Directive 2006/48/EC. Such authorisation creates access to central bank liquidity for those CCPs. On the other hand, other member states do not require CCPs to obtain such an authorisation.

i. Is there a need for measures to facilitate the access of CCPs to central bank liquidity facilities?

ii. If your answer to i. is yes, what are the measures that should be considered and why?

EACB Response

The EACB considers that is important that CCPs have access to central bank liquidity in order to safeguard liquidity and reduce any systemic risk for the members and their clients. For this reason, we consider that -like Eurex which is currently the only CCP authorised as a credit institution- other CCPs should also fulfil the same requirements. This will also preserve a level-playing field within the EEA.

A compulsory authorisation as credit institution, a guarantee from the State or (partial) ownership by the State and resolution planning for CCPs would be adequate measures in that regards. Next to that it could also be considered that CCPs deposit their cash at accounts with the central bank. This would mitigate the risk of losses.

In general, we would also like to take the opportunity to note that as explained in detail in Q.2.2 it is important to provide more access to clearing for smaller counterparties (pension funds, small banks, insurance companies for example). Also, as we note in Q 1.5. in order to ensure for a levelled access to CCPs, rules in respect of initial margin requirements should be uniform between CCPs. Capital requirements should not prevent banks to provide clearing services to smaller parties which have to clear/ want to clear their derivatives trades.

Question 1.2: Non-Financial Firms

Article 85(1)(b) states that: " The Commission shall.....assess, in coordination with ESMA and the relevant sectoral authorities, the systemic importance of the transactions of non-financial firms in OTC derivatives and, in particular, the impact of this Regulation on the use of OTC derivatives by non-financial firms;"

Non-financial counterparties are subject to certain requirements of EMIR. However, such counterparties will not be subject to the requirements to centrally clear or to exchange collateral on non-centrally cleared transactions provided that they are not in breach of predefined thresholds, in accordance with Article 10 of EMIR. Further, it is recognised that non-financial counterparties use OTC derivative contracts in order to cover themselves against commercial risks directly linked to their commercial or treasury financing activities. Such contracts are therefore excluded from the calculation of the clearing threshold.

(a) i. Are the clearing thresholds for non-hedging transactions (Article 11, Regulation (EU) No 149/2013) and the corresponding definition of contracts objectively measurable as reducing risks directly relating the commercial activity or treasury financing activity (Article 10, Regulation (EU) No 149/2013) adequately defined to capture those non- financial counterparties that should be deemed as systemically important?

ii. If your answer to question i. is no, what alternative methodology or thresholds could be considered to ensure that only systemically important non-financial counterparties are captured by higher requirements under EMIR?

EACB Response

The EACB is supportive of an internationally consistent definition of non-financial counterparties (NFC)(i.e. non-systematically important counterparties.

Obtaining information from NFC on their status has indeed proved to be a very difficult exercise. For this reason it would be advisable to establish a register which collects the notifications of NFC+ and makes them available to all derivative parties (for example by means of a global database maintained by an official organisation). This would allow parties to be able to identify NFC+, to conclude that all other NFCs are NFC- and would ensure transparency, legal certainty and consistency of data for all parties. Otherwise, parties only rely on the information and documentation of their counterparties with all the inconsistencies between parties this might entail. The EACB would like to take this opportunity to advocate the exclusion from EMIR central clearing and margin requirements of all non- systemically important firms – not just the NFC - (See also our answer under Q 2.2).

(b) Please explain your views on any elements of EMIR that you believe have created unintended consequences for non-financial counterparties? How could these be addressed?

EACB Response

In our view, central clearing could have unintended consequences in terms of liquidity fragmentation. Liquidity will move on to centralised CCP and there will be move away from bilateral trading. This has huge consequences (among others regarding pricing and liquidity) for smaller non financial counterparties (NFC-) (but also smaller cooperative banks and building societies for example) as it will leave them with more difficult access to hedging possibilities. Such liquidity concentration is already evidenced in the market and will further develop when the clearing requirements kicks in.

In addition, the reporting obligation under EMIR has also been problematic for NFC. We are of the view that excluding NFC- from reporting and other risk mitigation measures too could be an option. Such obligations could be fulfilled by their counterparties solely (i.e. FCs and NFC+, if relevant) when they trade with NFC- by introducing a single sided reporting obligation[1], valuation statements (instead of portfolio reconciliations) to be sent to NFC-, timely confirmation obligations for the confirmation generators and compulsory dispute resolutions for FCs and NFC+ when they trade with NFC- based on international models (for example as proposed by ISDA) rather than a bilateral agreement between the relevant parties. Please also refer to the parts dealing with reporting and risk mitigation measures for further details and arguments.

(c) Has EMIR impacted the use of, or access to, OTC derivatives by non- financial firms? Please provide evidence or specific examples of observed changes.

EACB Response

The use of and access to OTC derivatives by NFCs have substantially and considerably decreased. This is due to several factors among others:

- the complexity of the regulations for parties that may not have sufficient legal knowledge;
- the increase of the price of the OTC derivatives - such products have become very costly - due to the decrease of liquidity in the derivative markets;

[1] We understand that the industry is divided on this point.

- the pass through of costs incurred by FCs in connection with the implementation of EMIR (IT costs, operational setup, project management, repapering, legal support, etc.); and
- the leverage ratio impact under Basel III.

When NFC clients need to pay more or are not willing to comply with EMIR, no OTC derivative trading would be possible for NFCs. As no alternative to (OTC) derivatives for NFCs exists to be able to hedge the risks incurred in connection with currencies, commodities or interest rates, this means that such parties are not able to hedge their risks. When no hedging is possible, this involves risks for NFCs which will be taken into account by credit institutions when considering the creditworthiness of NFCs. This leads to a direct impact on the financing possibilities for NFCs because credit institutions account non-hedging as an increased counterparty risk. The decrease of financing possibilities has a direct impact on the economy and the customers' interest.

The situation is similar for smaller FCs and is also a very worrying trend. Liquidity has gone down materially and it has become far more difficult to execute larger trades.

As regards Basel III and the leverage ratio rules the issue is that cleared trades are exempted while the bilateral trading (with however margin requirements) is not. In addition, when transactions are cleared through a clearing broker, the back transactions between the clearing broker and the client (principal-to-principal model in Europe) are also not exempted from the Basel III leverage ratio rules. These two (no exemptions) lead to very high and disproportionate capital requirements for OTC transactions that do not fall under the clearing requirements, small clients/derivative parties that do not fall under the clearing obligations and parties that need to involve a clearing broker in order to be able to clear derivative transactions. The non-equitable capital requirements mean that the pricing of bilateral transactions and client cleared transactions is high and have direct consequences for the liquidity and the European Union/global economy. When the price is high and the liquidity is low this means fewer possibilities for parties to hedge their positions via derivative instruments. To address this issue client clearing exposure should be held outside the Basel III leverage ratio rules and the initial margin requirements should be excluded from the rules as well. This would ensure for an equitable balance between the cleared world and the bilateral world.

Question 1.3: CCP Colleges

Article 85(1)(c) states that: " The Commission shall....assess, in the light of experience, the functioning of the supervisory framework for CCPs, including the effectiveness of supervisory colleges, the respective voting modalities laid down in Article 19(3), and the role of ESMA, in particular during the authorisation process for CCPs."

In order for a CCP established in the Union to provide clearing services, it must obtain authorisation under Article 14 of EMIR. EMIR introduced a college

system for the granting of such authorisation, which has, to date, been used for the process of authorisation of sixteen CCPs. The College comprises members from relevant competent authorities, relevant members of the European System of Central Banks and ESMA.

- **(a) What are your views on the functioning of supervisory colleges for CCPs?**
- **(b) What issues have you identified with respect to the college system during the authorisation process for EU CCPs, if any? How could these be addressed?**

EACB Response

N/A

Question 1.4: Procyclicality

Article 85(1)(d) states that: " The Commission shall....assess, in cooperation with ESMA and ESRB, the efficiency of margining requirements to limit procyclicality and the need to define additional intervention capacity in this area."

CCPs authorised in the Union must take into account potential procyclical effects when calculating their margin requirements. The specific factors that must be considered to avoid disruptive movements in margin calculations are provided for under Article 41 EMIR and Article 28 of Commission Delegated Regulation (EU) No 153/2013.

i. Are the requirements under Article 41 EMIR and Article 28 Regulation (EU) No 153/2013 adequate to limit procyclical effects on CCPs' financial resources?
ii. If your answer to i. is no, how could they be improved?

EACB Response

Yes. However, we would like to make the following observations:

As far as the margin requirements are concerned and in order to improve the access to clearing, not only cash but other instruments should be possible to be posted to the CCPs. If CCPs have direct access to liquidity from central banks, they should be able to "transform" financial instruments received as collateral with cash.

In addition, the repo markets should remain for all parties a viable instrument to transform collateral and to ensure liquidity. Repo provides a source of short-term capital, facilitating liquidity and, therefore, efficient and stable financial markets. For example, a pension fund should be able to deposit financial instruments to comply with (initial and variation) margin requirements. Through a repo the financial instruments can be transformed into cash if and when necessary. In that case the pension funds do not have to sell financial instruments in their portfolio to obtain cash. By having such possibilities, the negative consequences on the return on their portfolio can be minimised as much as possible. However, the repo market faces more and more difficulties due to Basel III requirements and other (future) laws and regulations (among others future requirements under the Securities Financing Transparency Regulation). If for instance the use of collateral in the repo transactions is regulated, possibly including a mandatory minimum haircut, we are concerned this may restrict market participants' ability to make appropriate risk-based determinations regarding collateral. Higher mandatory haircuts may seem appropriate from a systemic risk perspective, but would reduce or eliminate the attractiveness of the transaction for the participants and the likely reduction in market liquidity could outweigh any possible benefits.

(b) i. Is there a need to define additional capacity for authorities to intervene in this area?

ii. If your answer to i. is yes, what measures for intervention should be considered and why?

EACB Response

N/A

Question 1.5: CCP Margins and Collateral

Article 85(1)(e) states that: " The Commission shall....assess, in cooperation with ESMA the evolution of CCP's policies on collateral margining and securing requirements and their adaptation to the specific activities and risk profiles of their users."

Collateral collected by way of initial and variation margin requirements is the primary source of financial resources available to a CCP. Title IV of EMIR and Commission Delegated Regulation (EU) No 153/2013 provide detailed requirements for the calculation of margin levels by CCPs as well as defining the assets that may be considered eligible as collateral.

(a) i. Have CCPs' policies on collateral and margin developed in a balanced and effective way?

ii. If your answer to i. is no, for what reasons? How could they be improved?

EACB Response

No. In general CCPs apply different policies with respect to margin requirements. Eligible margin should not constitute a competition element between CCPs.

For this reason, margin eligibility and valuation models for CCPs should be pre-determined and uniformed under EMIR.

(b) i. Is the spectrum of eligible collateral appropriate to strike the right balance between the liquidity needs of the CCP and its participants?

ii. If your answer to i. is no, for what reasons? How could it be improved?

EACB Response

Please refer to our answer under (a) above.

PART II

General Questions

Question 2.1: Definitions and Scope

i. Are there any provisions or definitions contained within Article 1 and 2 of EMIR that have created unintended consequences in terms of the scope of contracts or entities that are covered by the requirements?

ii If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response

Yes.

First of all, as already stated above the confirmation of the status of non-financial counterparties (NFC- or NFC+) has proved to be and will remain a very difficult exercise. In addition there is no 100% certainty that the parties will provide the information and/ or will provide correct information. A public database/register collecting all such information and accessible to all parties would create transparency, consistency and legal certainty for all parties. The results from notification regarding NFC+ status should be published in order for all parties not to have to collect the information and be able to conclude that the rest of parties are NFC-. In addition exempted entities and pension funds should have the obligation to notify their status to the relevant regulators and such information should be published for all parties to be able to access the information in order create legal certainty and consistency.

Moreover, the exemption of private individuals from the scope of EMIR but the inclusion of individuals acting for commercial purposes has created complexity and difficulties in collecting the correcting information. We would propose that Private individuals irrespective of whether they act for private or commercial purposes should be excluded from the scope of EMIR. However as already considered above for NFC-, unilateral and uniform obligations for FC and NFC+ when trading with such counterparties should be created.

The definition of OTC derivatives with a link to MiFID has led to undesirable consequences as regards, for example FX spot transactions. In this context the EACB looks forward to the result of the work done in this respect in the context of MIFID 2. In general, the EACB would ask that alignment is sought between the definitions in MiFID and EMIR. This means that - next to derivatives traded on a regulated market - derivatives traded on a MTF or OTF should also not be considered OTC derivatives.

It should be clarified that structured trades and derivatives embedded in other products do not fall under the scope of EMIR (among others for reporting obligations) since the derivatives aspect of such instruments is only a minor point when qualifying the whole instrument and assessing how it should be treated (which should be done on the basis of the main focus of such instrument, eg loan, insurance product, etc.)

Lastly, we would like to report that some of our largest members have AIFM clients and they consider that registered should be exempted from clearing and margin requirements under EMIR The latter manage smaller funds. Compliance with the EMIR requirements as FC are too heavy for these smaller AIFMS. For example the requirements of central clearing, mandatory exchange of collateral and to mark-to-market the value of their outstanding contracts on a daily basis is not well suited for these smaller AIFMs. These burdensome EMIR requirements hinder smaller funding initiatives in the market. The EMIR requirements for NFC below the clearing threshold are better suited for these smaller AIFs. An easy solution to address this problem would be to delete registered AIFMs in the definition of FC in article 2 paragraph 8 of EMIR.

Question 2.2 - Clearing Obligations

(a) i. With respect to access to clearing for counterparties that intend to clear directly or indirectly as clients; are there any unforeseen difficulties that have arisen with respect to establishing client clearing relationships in accordance with EMIR?

ii If your answer to i. is yes, please provide evidence or specific examples.

How could these be addressed?

EACB Response:

Yes, it is worth noting that small and medium-sized FCs have severe problems to enter into clearing relationship, due to both cost and availability issues. Indirect or client clearing offerings have not proven to be successful due to legal and practical challenges. Therefore a small number of clearing members are able to offer to clear on behalf of smaller counterparties but at a cost totally disproportionate compared to the business of smaller players.

Should no solution become available, small banks, building societies and financial firms will de facto not be able to keep an efficient risk management activity (particularly for the interest rate risk) by means of trading OTC derivatives to hedge their positions. This hedging is a vital part of the retail and real economy focused business of cooperative banks, providing an essential managing tool that then allows those banks to effectively finance individuals and SMEs. Due to these problems, the clearing obligation is unintentionally forcing smaller financial firms out of the derivatives markets. This reduces competition and shifts market balance. Pushing these companies out of business would deteriorate the credit conditions of SME segment even further and thus jeopardize the fragile recovery of European economies. This would be inconsistent with the Capital Market Union policy agenda aiming to remove barriers to the free flow of capital in Europe and the variety of other policy makers' positive initiatives to stimulate economic growth in Europe.

With this in mind, we suggest to extend EMIR Article 10 in order to provide for a threshold for the clearing obligation and the total exemption in the calculation of this threshold of OTC derivative contracts which are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity of the NFCs or of that group (e.g. with hedging purposes) set for non-financial counterparties to financial counterparties which likewise use these contracts only for hedging purposes (See also our response to Q 1.2.). In that regard, it should be taken in account that these bilateral OTC derivative contract (not cleared) would be collateralised, ensuring the risk mitigation.

As an alternative to the extension of Article 10 to certain smaller FC, we would propose the following:

- In line with Article 10.3 all hedging / protection contracts[2] could be fully exempted, but only for small institutions (below a balance sheet size threshold – indicatively this could be set at € 5 billion). This would be most in line with emerging practice in other major jurisdictions - see below.

[2] In accordance to Article 10 of DELEGATED REGULATION (EU) No 149/2013 which establishes the criteria for establishing which OTC derivative contracts are objectively reducing risks:

1. An OTC derivative contract shall be objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity of the non-financial counterparty or of that group, when, by itself or in combination with other derivative contracts, directly or through closely correlated instruments, it meets one of the following criteria:

(a) it covers the risks arising from the potential change in the value of assets, services, inputs, products, commodities or liabilities that the non-financial counterparty or its group owns, produces, manufactures, processes, provides, purchases, merchandises, leases, sells or incurs or reasonably anticipates owning, producing, manufacturing, processing, providing, purchasing, merchandising, leasing, selling or incurring in the normal course of its business;

(b) it covers the risks arising from the potential indirect impact on the value of assets, services, inputs, products, commodities or liabilities referred to in point (a), resulting from fluctuation of interest rates, inflation rates, foreign exchange rates or credit risk;

(c) it qualifies as a hedging contract pursuant to InternationalFinancial Reporting Standards (IFRS) adopted in accordancewith Article 3 of Regulation (EC) No 1606/2002 of the European Parliament and of the Council (1).

- As an alternative to the total exemption we would propose to set for small institutions which trade OTC derivative contracts only for hedging purpose a clearing threshold of EUR 500 million in gross notional value for all type of derivatives.

The EACB also draws to the Commission's attention that the current EU regime under EMIR is far more burdensome for small banks than in other major jurisdictions. The principal example, of course, is the US, where the equivalent central clearing regime introduced under the Dodd Frank Act explicitly exempts categories of small banks that are end-users of derivatives for hedging purposes from the clearing obligation. This was effected by a CFTC Final Rule made in 2012, following consultation, with an exemption threshold of US$ 10 billion. The CFTC's documentation[3] also explains why such exemption is desirable and does not compromise the objectives of derivatives reform. In Australia, currently proposed rules[4] on mandatory clearing will exempt financials below a high clearing threshold (AUD 100 billion gross notional outstanding derivatives). In Japan, the range of financial entities subject to mandatory clearing is also narrower. In Canada, regulatory authorities are prepared to contemplate introducing some exemptions for small banks after reviewing the early information available from trade repositories. The situation is similar in Switzerland with FinfraG (Finanzmarktinfrastrukturgesetz) exempting smaller financial counterparties from connecting to a central counterparty.[5] The global trend is clearly away from imposing disproportionate clearing obligations on small financials, and - in line with the new direction from First Vice-President Timmermans and Commissioner Lord Hill - we urge the Commission to do the same.

Other aspects that should also be taken into account in order to facilitate indirect clearing arrangements and that have proven their imperfections and do not work are capital requirements under CRD and Basel III because indirect clearing leads to double capital requirements.[6] When the price is high and the liquidity is low this means less possibilities

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[3] http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/federalregister081313.pdf
See also: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-17291a.pdf

[4] http://download.asic.gov.au/media/3252197/cp231-published-28-may-2015.pdf

[5] http://www.finfrag.ch/en/ . It is expected that FinfraG will come into effect towards the beginning of 2016. FinFrag introduces 4 different counterparty types: In comparison with the EU regulation, an additional category has been introduced which is small financial counterparties. This exempts smaller financial counterparties from connecting to a central counterparty – similarly to the end user exception of Dodd Frank regulation in the United States. The thresholds for counterparty classifications are not known yet. It is expected however, that the thresholds will be similar to the Dodd Frank and EMIR.

[6] In particular, as already noted above, clearing is exempted from the leverage ratio rules under Basel III, while the bilateral trading (with however margin requirements) is not exempted. In addition when transactions are cleared through a clearing broker, the back transactions between the clearing broker and the client (principal-to-principal model in Europe) are also not exempted from the Basel III leverage ratio rules. These two (no exemptions) lead to the fact that capital requirements are very high and not proportionate to the cleared transactions. This has direct impact for OTC transactions that do not fall under the clearing requirements, small clients/derivative parties that do not fall under the clearing obligations and parties that need to involve a clearing broker in order to be able to clear derivative transactions. The non-equitable capital requirements mean that the pricing of bilateral transactions and client cleared transactions is high and have direct consequences for the liquidity and the European Union/global economy.

for parties to hedge their positions via derivative instruments. To address this issue client clearing exposure should be held outside the Basel III leverage ratio rules and the initial margin requirements should be excluded from the rules as well. This would ensure for an equitable balance between the cleared world and the bilateral world.

(b) i. Are there any other significant ongoing impediments or unintended consequences with respect to preparing to meet clearing obligations generally in accordance with Article 4 of EMIR?

ii If your answer to i. is yes, please provide evidence or specific examples.

How could these be addressed?

EACB Response:

Yes, please see our response to (a) above. In any case, given that the risk is already present that some smaller banks have no certainty of finding a clearing arrangement allowing them to comply with EMIR we would consider that at least some more time would be necessary to explore solutions before mandatory clearing comes in.

Furthermore, the frontloading requirements for category 1 and category 2 parties (expected to be the rule in the RTS) will lead to legal uncertainties, inconsistencies, pricing issues and monitoring/operational issues (IT setup, etc.). Thus, it would be favourable to delete the frontloading requirements – in particular given the fact that ESMA itself tried to limit it -to the extent possible- by defining the remaining maturities in a way that only very few transactions will be covered by the frontloading requirement.

Moreover, in order to avoid monopoly situation, we recommend that a product not be subject to mandatory clearing until at least two or three CCPs can offer clearing for that product with such CCPs able to ensure for liquidity. At present, even though more CCPs are able to clear, it is the current experience that one CCP has the monopoly or at least is able to provide liquidity (LCH).

Moreover, the centralisation of clearing via CCPs via clearing versus the bilateral clearing world results in a concentration of risks due to the small number of CCPs on the one hand and a small number of clearing brokers offering this service to a broad range of clients on the other. This risk needs to be addressed. It is therefore crucial to implement measures that mitigate the risk of potential CCP failure to protect against systemic risks. A possible solution is to have for market participants the ability to port/transfer or re-establish position using another CCP which would again require that no clearing mandate be put in place unless there are at least two CCPs available to clear that particular swap. The fungibility of contracts between CCPs should allow for smooth transfer of positions. This will allow all market participants to have optionality to re-establish positions at a viable CCP, use other instruments to hedge risk or in some cases remain neutral if the credit exposure to CCPs is viewed higher than the market exposure that is being hedged.

However, the porting feasibility in case of a clearing member defaulting is very uncertain. Some measures and/ or instruments should be pre-defined to facilitate the porting.

Moreover, the disclosure of clearing costs to EMIR clients as mentioned in article 38, paragraph 1 has more to do with investor protection instead of infrastructure. Next to that, this article is not limited to derivatives but to all financial instruments and also to retail clients. We consider that this is something that has already been included in the cost disclosure under MIFID II and should not be included in EMIR. This also prevents a fragmented approach.

In addition, it is necessary to establish processes which allow for a quick "de-listing" of no longer clearable products or otherwise ensure that counterparties are not effectively forced to stop transactions in products which are legally still subject to a clearing obligation but are no longer clearable.

Finally, EACB member banks experience that the application of the clearing obligation for non-deliverable forwards could not work in practice. These products are short term and low-risk transactions and imposing a clearing obligation would threaten liquidity and lead to an increase of the pricing. In this light, its members welcomed the decision of ESMA not to impose a clearing obligation on the NDF classes so far. The situation is similar with credit default swaps which are a very illiquid and very expensive market currently.

Question 2.3 - Trade reporting

i. Are there any significant ongoing impediments or unintended consequences with respect to meeting trade reporting obligations in accordance with Article 9 of EMIR?

ii. If your answer to i. is yes, please provide evidence or specific examples.

How could these be addressed?

EACB Response:

Yes, there have been some difficulties with regard to trade reporting as follows:.

- The reporting obligation has been difficult to implement due to problems in regulatory guidance and in the technical readiness at the trade repositories. The data provided is still lacking in quality regardless of the costly efforts made by the industry. Against this background and the reporting cost of a single transaction[7] it would be more proportionate to <u>introduce a threshold to the reporting obligation</u>.

[7] Includes for example the cost to obtain an LEI code, the work to gather all required information and the efforts to fill in the right details and the problems by the trade repositories to take in data and send a confirmation etc. The time needed to report one transaction has been varying from some 15 minutes to hours of work at one counterparty only.

The reporting requirements of non-financial counterparties under the clearing threshold are costly and very burdensome for these smaller companies. Because of their lacking expertise and necessary IT infrastructure they outsource these obligations to banks with often costs attached and involving legal documentation (reporting agreements). In this light, reconciliation with the banks' reporting has proved its non-efficiency . Non- financial counterparties have to ask for a LEI and to pay application costs and an annual fee. Not all non-financial counterparties have a LEI code (especially the smaller ones), and financial counterparties cannot force them to obtain one. We consider that the use of LEI code should not become mandatory in transaction reporting of the smaller NFC under the clearing threshold. Different alternative solutions could be applied for these counterparties which would preserve and facilitate the transparency requirements (e.g, no LEI requirement; internal codes or BIC codes should suffice). Most of the EACB members are in favour of a less burdensome solution for non-financial counterparties under the clearing threshold like the one followed in the Dodd Frank Act Title VII (i.e. single-sided reporting obligation): Under DFA Title VII, registered swap dealers are doing the reporting and transposing the same principles under EMIR would be an improvement, no burdensome for non-financial counterparties under the threshold and would ensure for a global level playing field. <u>Banks instead of their non- financial counterparties could be the reporting party to the trade repositories.</u> This would also make it easier to align the EMIR reporting to the MIFID reporting, because the MIFID reporting is limited to investment firms. Article 9 of EMIR could be focused on financial counter parties and CCPs. Non-financial counterparties (at least under the threshold) could be left out.

- <u>We would welcome a deletion of Art. 5 (4) of Regulation 1247/2012. We do not see the benefit of backloading transactions that were already terminated by 12 February 2014.</u>
- Reporting obligations regarding listed derivatives should not apply. This obligation should enter into force under Mifid II/MiFIR. Besides EMIR several other initiatives (e.g. Solvency II, ECB money market reporting, MiFID II) also require data on derivatives, resulting in the obligation for financial institution to produce many reports to different instances with slightly different data fields. There is an urgent need to streamline these many different requirements. The EMIR reporting obligation is in force and requires a huge amount of data on all possible derivatives contacts shortly after conclusion, novation or termination. Instead of separate reports from the companies using derivatives, trade repository data should be used. Regulators and the ECB should participate in the review to make sure that the data will be of good quality and contains the right elements for their purposes. Trade repositories are also very likely capable to put together needed reports for many purposes. Streamlined reporting would be a major cost-saver for the industry and for the regulators. In this context most of our members suggest the possibility to have one central Trade Repository with no commercial objectives and one locket for all reporting obligations should be considered (see our response to Q 2.7)

Question 2.4 - Risk Mitigation Techniques

i. Are there any significant ongoing impediments or unintended consequences with respect to meeting risk mitigation obligations in accordance with Articles 11(1) and (2) of EMIR?

ii. If your answer to (i) is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

As already stated above, rather than imposing an obligation for parties to bilaterally agree details in order to comply with risk mitigation mechanisms such as portfolio reconciliations and dispute resolutions, the relevant RTS should focus on a unilateral obligation for financial counterparties and NFC+ to ensure for these principles. The portfolio reconciliation requirements should be replaced with an obligation for FCs and NFC+ to send valuation statements to NFC- with a right for such NFC- to contest the statements, dispute resolutions should be made mandatory under EMIR referring to the methods developed by recognized industry parties (ISDA for example) without the need to pre-agree the method and timely confirmation requirements should be imposed to FCs and NFC+ solely. This would ensure for legal certainty, certainty of application of the rules, uniformity/consistency and would avoid administrative burden for parties to repaper their documentation in this view. In addition not only EEA NFCs are concerned by these rules but also non-EEA NFCs. For these non-EEA parties, many more difficulties are faced to ensure for the agreement on risk mitigation rules because such parties estimate that EMIR does not apply to them. To facilitate the process and ensure for legal certainty and uniform application, the one-sided requirements are desirable.

Question 2.5 - Exchange of Collateral

i. Are there any significant ongoing impediments or unintended consequences anticipated with respect to meeting obligations to exchange collateral in accordance with Article 11(3) under EMIR?

ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

The EACB considers that the obligation for clearing members to offer individually segregated accounts to clients is not suited to the retail market. Retail clients do not put enough business through to justify the cost of maintaining these accounts. Indeed, the costs of building and maintaining individual segregation are high and the extra costs of the CCP must be added. The costs are far beyond what is acceptable for retail clients and therefore they will not opt for an ISA and choose for omnibus segregation. We think that banks should not be obliged to offer costly ISA's in the retail market knowing they are not suitable and too expensive for retail clients. Moreover, the cost of a ineffective and non-used ISA system will have to be born by all (retail) clients. Therefore, because of the operational costs, individual segregation will only be suited for bigger financial and non-financial counterparties. However article 39, paragraph 5 oblige clearing members to offer individual segregation to all clients as meant in EMIR. There is also no limitation to derivatives but it extends to all financial instruments (the EACB supposes during the T + 2 period) and all parties subject to EMIR irrespective of their size and trading volume. We could therefore propose to limit the application of article 39 paragraph 5 to financial counterparties and non- financials above the clearing threshold. We would also propose to limit the ISA requirement to derivatives. There is no need for the obligatory offering of an ISA for other financial instruments. Segregation requirements are applicable on the basis of MIFID and with regard to the settlement (T+2) delivery versus payment is used.

Question 2.6- Cross-Border Activity in the OTC derivatives markets

(a) i. With respect to activities involving counterparties established in third country jurisdictions; are there any provisions or definitions within EMIR that pose challenges for EU entities when transacting on a cross-border basis?

ii. If your answer to (i) is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

EMIR has a huge extra-territorial impact which impact the bigger members of EACB in an important way. The EACB would therefore consider that until the moment the rules regarding equivalence are crystalised by the European Commission, EMIR should only apply to EEA parties. The first step should obviously be the EEA and when equivalence is established then EMIR can be applied to non-EEA parties transacting with EEA parties. At the same time, the extra-territorial effect should be implemented within a longer term than for EEA parties.

In addition, the equivalence requirements to obtain exemptions for the clearing/margin requirements for intragroup transactions between a EEA entity and a non-EEA entity has no raison d'être. Intragroup transaction exemptions should be subject to the demonstration of certain conditions (centralized risk management, etc.) but the equivalence requirements have no raison d'être insofar as the prevention of systemic risks are concerned. Generally entities enter into back-to-back intragroup transactions or other intragroup transactions in order to precisely centralize the treasury and market risks with a parent entity or affiliated entity. No differences of treatment should apply between EEA and non-EEA intragroup transactions in respect of exemptions. Therefore we propose to delete the restriction on equivalence requirements as far as intragroup transactions with non EEA group entities are concerned.

Moreover, an implementing act of equivalence should also be possible to apply on transactions between two non EEA branches of EEA banks. Especially in these situations a mechanism is needed to avoid duplicative and conflicting rules. Therefore we propose to delete the restriction on possible equivalence as mentioned in article 13, paragraph 3 last part commencing with "where……".

In general, we would consider that it is better that the equivalence recognition applies on a regime-by-regime basis and not on a rule-by-rule basis to facilitate the equivalence procedures.

(b) i. Are there any provisions within EMIR that create a disadvantage for EU counterparties over non-EU entities?

ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

See our response above under (a).

Question 2.7 Transparency

i. Have any significant ongoing impediments arisen to ensuring that national competent authorities, international regulators and the public have the envisaged access to data reported to trade repositories?

ii. If your answer to i. is yes, please provide evidence or specific examples.How could these be addressed?

EACB Response:

The LEI requirements has created many difficulties (see our response above).

The services provided by Trade Repositories are costly services and the fees and services may be subject to unilateral and inequitable amendments for reporting parties. e.g. recently clients of a TR have been confronted already with a 100 % rise of fee starting immediately. Some controls/safeguards should be imposed by regulators in this view. Most of the EACB members support that the solution of one central Trade Repository with no commercial objective for all reporting obligations should also be considered. This could ensure for a general, consistent and transparent reporting tool and no reconciliation issues with other Trade repositories. Such as Central not for profit Trade Repository could also be used for other regulatory reporting for example Under MIFID (MIFIR in the future) and the coming Securities Financing Transparency Regulation.

Confidentiality and bank secrecy obligations which may conflict with reporting obligations are still not addressed at international level. These conflicting rules should be solved between regulators at international level in order for parties to be able to report and comply with their local requirements without the risk to incur liabilities and fines due to local confidentiality and bank secrecy rules. By way of example we would like to refer to countries like Argentina, Brazil, Indonesia, Israel and South Korea which have specific restrictions on submitting counterparty details. Until the moment the problem is solved parties should be able to report on a mask basis (meaning without counterparty details in case of transactions with non-EEA counterparties in jurisdictions where confidentiality rules restrict/ prohibit disclosure of such information). Otherwise, regulatory reporting of counterparty details should be allowed with the consent of the counterparty on an internationally accepted manner (like the ISDA 2013 EMIR Reporting Protocol).

Question 2.8 Requirements for CCPs

(a) i. Are there any significant ongoing impediments or unintended consequences with respect to CCPs' ability to meet requirements in accordance with Titles IV and V of EMIR?

ii. If your answer to (i) is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response

Yes. We have already mentioned above in a different set of questions that:

- It is important that CCPs have access to central banks liquidity in order to preserve liquidity and reduce any systemic risks for the members and their clients.
- CCPs apply different policies in respect of margin requirements. Eligible margin should not constitute a competition element between CCPs. Margin eligibility and valuation models for CCPs should be pre-determined and uniformed under EMIR.

(b) i. Are the requirements of Titles IV and V sufficiently robust to ensure appropriate levels of risk management and client asset protection with respect to EU CCPs and their participants?

ii. If your answer to i. is no, for what reasons? How could they be improved?

EACB Response

N/A

(c) i. Are there any requirements for CCPs which would benefit from further precision in order to achieve a more consistent application by authorities across the Union?
ii. If your answer to i. is yes, which requirements and how could they be better defined?

EACB Response

N/A

Question 2.9 - Requirements for Trade Repositories

i Are there any significant ongoing impediments or unintended consequences with respect to requirements for trade repositories that have arisen during implementation of Titles VI and VII of EMIR, including Annex II?

ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

Yes. Trade repositories are commercial organisations and may amend their services and fees on a unilateral basis. This may hamper parties facing reporting obligations. Some controls/safeguards should be imposed by regulators in this view. An alternative (as suggested by most of the EACB membership) could be to have one central Trade Repository with no commercial objectives and one locket for all reporting obligations. This would ensure for a general, consistent and transparent reporting tool.

Question 2.10 Additional Stakeholder Feedback

i. Are there any significant ongoing impediments or unintended consequences with respect to any requirements or provisions under EMIR and not referenced in the preceding questions that have arisen during implementation?

ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EACB Response:

N/A

Contact:

The EACB trusts that its comments will be taken into account.

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