



European Securities and
Markets Authority

Reply form to the Consultation Paper on the Clearing Obligation under EMIR (no. 1)



Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the questions listed in the Consultation Paper on the Clearing Obligation under EMIR (no. 1), published on ESMA's website.

Comments are most helpful if they:

- respond to the question stated;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

To help you navigate this document more easily, bookmarks are available in "Navigation Pane" for Word 2010 and in "Document Map" for Word 2007.

ESMA will consider all comments received by **18 August 2014**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

How to use this form to reply

Please note that, in order to facilitate the analysis of the responses, ESMA will be using an IT tool that does not allow processing of responses which do not follow the formatting indications described below.

Therefore, in responding you are kindly invited to proceed as follows:

- use this form to reply and send your response in Word format;
- type your response in the frame "TYPE YOUR TEXT HERE" and do not remove the tags of type <ESMA_QUESTION_1> Your response should be framed by the 2 tags corresponding to the question; and
- if you have no response to a question, do not delete the tags and leave the text "TYPE YOUR TEXT HERE" between the tags.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.



Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Legal Notice'.

Who should read this paper

All interested stakeholders are invited to respond to this consultation paper. In particular, responses are sought from financial and non-financial counterparties of OTC derivatives transactions which will be subject to the clearing obligation, as well as central counterparties (CCPs).



General information about respondent

Name of the respondent	ASSOSIM – Associazione Italiana Intermediari Mobiliari
Are you representing an association?	Yes
Activity	Financial Services
Country/Region	Italy



Introduction

Please make your introductory comments below:

<ESMA_COMMENT_1>

The Italian Financial Intermediaries Association (ASSOSIM) welcomes the opportunity to provide the views of its members on the analysis presented by ESMA in this consultation paper. ASSOSIM represents the majority of financial intermediaries acting in the Italian Markets and has nearly 80 members represented by banks, investment firms, branches of foreign brokerage houses, active in the investment services industry, mostly in primary and secondary markets of equities, bonds and derivatives, for some 82% of the Italian total trading volume. Please, note that the present document was drafted in cooperation with the Italian Banking Association (ABI).

ASSOSIM notes that the recent months have been extremely busy with important and extensive ESMA/joint ESAs consultations around market discipline and derivatives markets. Our members active in the derivatives markets were not always in a position to analyse properly the effects of these proposals, making suitable phase-in periods even more important than previously thought, as part of these analysis will be run in the forthcoming period. Thus, we consider that ESMA should maintain a flexible approach with its rules, also and especially when implementation will be approaching.

In conclusion, ABI and ASSOSIM value importantly the decision to follow a bottom-up approach for the clearing obligation and, in general terms, welcomes the phase-in timeframe proposed.

<ESMA_COMMENT_1>

1 The clearing obligation procedure

Question 1: Do you have any comment on the clearing obligation procedure described in Section 1?

<ESMA_QUESTION_1>

We agree with the clearing obligation procedure described and are pleased to acknowledge that ESMA has decided to group derivatives into five asset classes, consulting stakeholders on the basis of each derivatives' class.

<ESMA_QUESTION_1>

2 Structure of the interest rate derivatives classes

2.1 Characteristics to be used for interest rate derivative classes

Question 2: Do you consider that the proposed structure defined here for the interest rate OTC derivative classes enables counterparties to identify which contracts fall under the clearing obligation as well as allows international convergence? Please explain.

<ESMA_QUESTION_2>

Yes, we consider that the proposed structure for the interest rate OTC derivative classes enables counterparties to identify which contracts are subject to the clearing obligation and allows international convergence.

However, we suggest ESMA to complete the definition provided for the products – which is exactly in line with Dodd-Frank Act – by explicitly stating that those deals/trades which are not accepted for clearing by CCPs are automatically excluded from the clearing obligation. Despite the latter is probably implicit in the framework, we deem important to make it explicit and clear in the final text of the RTS. For instance, it is not possible to centrally clear deals whose 'fixing' is computed 'in arrears' (*i.e.* at the end of the reference

period), neither those computed ‘up-front’ (i.e. at the beginning of the reference period), nor those trades which have a different workdays-holidays dates adjustment criteria.

<ESMA_QUESTION_2>

2.2 Additional Characteristics needed to cover Covered Bonds derivatives

Question 3: Do you consider that the proposed approach on covered bonds derivatives ensures that the special characteristics of those contracts are adequately taken into account in the context of the clearing obligation? Please explain why and possible alternatives.

Stakeholders (CCPs and covered bond derivatives users, in particular) are invited to provide detailed feedback on paragraph 38 above. In particular: what is the nature of the impediments (e.g. legal, technical) that CCPs are facing in this respect, if any? Has there been further discussions between CCPs and covered bond derivatives users and any progress resulting thereof?

<ESMA_QUESTION_3>

On the basis of a preliminary analysis, in our opinion it seems difficult to find derivative contracts associated to covered bond programmes that satisfy all the conditions presented in paragraph 54 simultaneously. Furthermore, we believe that certain parts of paragraph 54 are not sufficiently clear or even applicable in all countries (e.g. paragraphs b, c, f).

Regarding **point 54 (a)**, (“*They are not terminated in case of default of the covered bond issuer*”), in general terms, in the context of covered bonds, a derivative is designed to survive the insolvency of the covered bonds issuer.

Therefore, in case of default of the latter, the source of payments switches to the cover pool, on which the derivative counterparty has a preferential claim alongside with the covered bondholders.

Hence, as the purpose of the market participants is to avoid any termination of the derivative because of the issuer default, the concept of ‘default’ could be narrowed down by inserting the specification “insolvency related default”, which is also in line with the views of the European Covered Bond Council.

As it regards **point 54 (b)**, (“*The counterparty to the contracts, which counterparty is not the cover pool or the covered bond issuer, ranks at least pari-passu with the covered bond holders*”), it is not clear what ESMA precisely means when it says: “...*which counterparty is not the cover pool or the covered bond issuer*”. If the meaning is that the covered bond issuer itself cannot act as swap counterparty, then we disagree, as certain covered bond programmes would not be compliant with that. Otherwise, should the meaning be that the swap counterparty is the issuer, then it should rank ‘junior’ to the note holders; accordingly, this should be checked in the specific waterfall of payments of each covered bond programme.

As far as **point 54 (c)** is concerned (“...*They are registered in the cover pool of the covered bond programme in accordance with national covered bond legislation*”), it is not clear what “registered” means as, in Italy, there is not such a (covered bond) legislation providing for a “registration” of the derivative contracts.

Regarding **point 54 (f)** (“...*The covered bond programme to which they are associated is subject to a legal collateralisation requirement of at least 102%*”), in Italy there is no legal requirement in terms of over collateralization (OC). The current legal requirement regards the collateralisation and compliance with the mandatory test to be performed on the programme. A possible alternative could be to consider a contractual OC of 102% as an alternative to a legal mandatory OC, as proposed by the European Covered Bond Council in occasion of previous consultations.

Finally, we strongly recommend a grandfathering period before any requirement becomes mandatory.

<ESMA_QUESTION_3>

2.3 Public Register

Question 4: Do you have any comment on the public register described in Section 2.3?



<ESMA_QUESTION_4>

We have no comments on this topic.

<ESMA_QUESTION_4>

3 Determination of the OTC interest rate classes to be subject to the clearing obligation

Question 5: In view of the criteria set in Article 5(4) of EMIR, do you consider that this set of classes addresses appropriately the systemic risk associated to interest rate OTC derivatives? Please include relevant data or information where applicable.

Please include relevant data or information where applicable.

<ESMA_QUESTION_5>

We consider that the set of classes addresses appropriately the systemic risk associated to IR OTC derivatives, especially as it recalls the Dodd-Frank Act classification and it allows to leave no room to arbitrage.

<ESMA_QUESTION_5>

4 Determination of the dates on which the obligation applies and the categories of counterparties

4.1 Analysis of the criteria relevant for the determination of the dates

Question 6: Do you have any comment on the analysis presented in Section 4.1?

<ESMA_QUESTION_6>

We have no comment to this question.

<ESMA_QUESTION_6>

4.2 Determination of the categories of counterparties (Criteria (d) to (f))

Question 7: Do you consider that the classification of counterparties presented in Section 4.2 ensures a smooth implementation of the clearing obligation? Please explain why and possible alternatives.

<ESMA_QUESTION_7>

In our opinion, the counterparties categorization proposed in article 2 of the draft RTS (page 91) shall be referred to asset classes, *i.e.* a counterparty should be allowed to fall into a specific category (*e.g.* Category 1) for an asset class for which it is a clearing member and to fall into another category (*e.g.* Category 2) for the other relevant cases already provided for in the text of the RTS.

We suggest ESMA to consider to adopt option 4 (on page 102) of “Conditions on the clearing membership”, which is surely a more complex but also a more precise and punctual approach to follow.

<ESMA_QUESTION_7>

4.3 Determination of the dates from which the clearing obligation takes effect

Question 8: Do you consider that the proposed dates of application ensure a smooth implementation of the clearing obligation? Please explain why and possible alternatives.

<ESMA_QUESTION_8>

First of all, we are grateful to ESMA for the new 'phase-in' framework, as it demonstrates that the analysis and comments presented by ABI and ASSOSIM, in September 2013, were taken into account (please, see our response to Q. 25 of ESMA's discussion paper ESMA/2013/926, DP on clearing obligation).

Secondly and in general terms, the proposed dates of application in the current CP seem to be calibrated in a way that ensures a smooth implementation for counterparties. However, compared to 2013, our member banks and financial intermediaries have now had some time to gather more evidence to base their decisions as to whether connect directly or indirectly to a CCP. Thanks to this – notwithstanding our positive feedback on the new framework designed by ESMA (*i.e.* the phase-in of categories 1, 2 and 3) – we present some considerations which are aimed at explaining why we recommend ESMA to take into consideration (i) the possibility of a further segregation of Category 2 and (ii) some other information gathered by our member banks.

Some of our member banks signalled the need to further differentiate the category of 'Financial Counterparties' (FC) within Category 2 as the concept of FC appears to be 'too broad' (or 'too generic') for the purposes of such categorization, as the entities it covers are very diverse, and, as it currently stands, the framework does not seem to appropriately reflect the application of the proportionality criterion. Hence, ABI and ASSOSIM believe that FCs should be further sub-categorised on the basis of thresholds and for each asset classes.

More in detail, Category 2 seems not to take into consideration the case of (a number of) financial intermediaries and banks that will not be directly connected to a CCP and which, most likely, will connect through a Clearing Member (CM) or become 'Clients'. As we tried to highlight in our response to ESMA's DP no. ESMA/2013/926 (see answers 20, 22, 25, 26 and 27), the calibration of the phase-in period should also take into account the case of indirectly connected participants and of small banks with a very modest volume/number of operations. In order to ensure a level playing field for market participants, the clearing obligation should be imposed only when consistent application of the various models of access to a CCP are equally ensured (as provided in art. 4 of EMIR). As represented in paragraph no. 133 of the CP, there are several banks (especially small cooperative banks) which do not have in place any clearing arrangements yet and are currently looking for an indirect access to CCP through a CM and this is consistent with ESMA statement "*more time is granted to counterparties to which access to clearing is more difficult*". The indirect access to CCPs is still (at the time of writing) difficult to achieve for small banks: as stated in paragraph 156, for the time being, the indirect clearing activity remains undeveloped and, as stated in paragraph 214, the offer of indirect client clearing is only at a very early stage.

As some of our member banks and financial intermediaries report (thanks to informal talks with entities which will potentially operate as CMs), the option of becoming Clients of a CM would imply large fees and overcollateralization by CMs, compared to the small size of local cooperative banks (namely, fees are considered to be too costly, not in absolute terms but in relative terms and proportionally to the size/volume of the operations of small cooperative banks and small financial intermediaries). This would make the option literally 'unbearable' to be pursued for those specific entities, in the absence of appropriate degree of competition among CMs.

As already highlighted in other occasions, in compliance with specific local laws and by-laws provisions, cooperative banks may use derivatives only for hedging purposes. According to such provisions, those cooperative banks which will not be able to access clearing through indirect agreements, nor as Clearing Members (or Clients of a Clearing Member), will *de-facto* be not able to keep an efficient risk management activity (particularly for the interest rate risk) by means of trading OTC derivatives.

To this end, in consideration of the small overall size/amount of the operations as well as the exclusive hedging purpose(s) of small intermediaries, we consider the distinction of counterparties into 3 categories to be 'sub-optimal', and **suggest ESMA to provide for a further segregation within Category 2 for FCs falling therein, specifically for banks characterised by a small size and low volume of OTC derivatives operations** dealt with for hedging purposes (as it is the case for example of



cooperative banks) because these banks – along with generally small banks and financial intermediaries – report difficulties in accessing clearing due to (i) CMs that sometimes do not accept (on the basis of quantitative criteria set by the CM itself) to provide indirect clearing arrangements to small banks and financial intermediaries, especially cooperative banks; (ii) expensive (in relative terms to the volume of operations of small banks) economic conditions (*i.e.*

. fees, margins/collateral) to access clearing. This type of banks and financial intermediaries should ideally be granted a period of 24 months in order to allow them a wider time frame to investigate as many clearing services' opportunities as possible, so that they could try to minimize the economic impact of the clearing service by finding on the market the most suitable clearing solutions/terms. Further to this, when comparing the considerations brought forward so far with the fact that (for instance) NFC+ (*i.e.* derivatives with purposes other than hedging) are provided with a phase-in of 3 years, and that the 'broader' (or 'more generic') category of 'FCs dealing in derivatives with hedging purposes' are provided with a phase-in of 18 months, it appears to us that the framework might be fine-tuned and need the slight re-balance suggested in the period highlighted in **bold** above.

<ESMA_QUESTION_8>



5 Remaining maturity and frontloading

Question 9: Do you consider that the proposed approach on frontloading and the minimum remaining maturity ensures that the uncertainty related to this requirement is sufficiently mitigated, while allowing a meaningful set of contracts to be captured? If not, please explain why and provide possible alternatives compatible with EMIR.

<ESMA_QUESTION_9>

Yes, we consider that the approach on frontloading and minimum remaining maturity is appropriate.

<ESMA_QUESTION_9>

6 OTC equity derivative classes that are proposed not to be subject to the clearing obligation

Question 10: Do you have any comment on the analysis on the Equity OTC derivative classes presented in Section 6?

<ESMA_QUESTION_10>

We have no comments on this topic.

<ESMA_QUESTION_10>

7 OTC Interest rate future and option classes that are proposed not to be subject to the clearing obligation

Question 11: Do you have any comment on the analysis on the OTC Interest rate future and options derivative classes presented in Section 7?

<ESMA_QUESTION_11>

We have no comments on this topic.

<ESMA_QUESTION_11>

Annex I - Commission mandate to develop technical standards

Annex II - Draft Regulatory Technical Standards on the Clearing Obligation

Question 12: Please indicate your comments on the draft RTS other than those already made in the previous questions.

<ESMA_QUESTION_12>

In the following response, we present some considerations around the topic of derivative contracts concluded to hedge one or more balance sheet items by hedge accounting activity.



ESMA's CP does not seem to take into account the IAS Accounting Principles' hedging purpose of contracts eligible for the clearing obligation and we regard this matter to be very important to be kept into account. Indeed, this element may cause serious difficulties in the management of those deals which are characterised by the hedging purpose compliant with the definition provided by the IAS Accounting Principles, *i.e.* those deals whose purpose is defined as "Cash Flow Hedge" and "Fair Value Hedge" (*i.e.* Hedge Accounting, HA).

Accordingly, and as we try to explain in the following paragraphs, **ABI and ASSOSIM ask ESMA to consider to carry out further in-depth analysis, along with the IASB and some CCPs, on the clearing of derivative contracts formally concluded to hedge one or more balance sheet items.** Meanwhile, **ESMA might consider to contemplate a suspension of the clearing obligation for hedge accounting (HA) derivatives.**

Indeed, when a transaction/contract is designed for hedging of one or more balance sheet items, on the basis of the IASB provision it is necessary to preserve over time this close relation between the derivative contract that hedges a position, and the position/financial instrument which is actually hedged (also, by respecting a pre-set range of the percentages of the Effective Test). In the case of bilateral transactions/contracts, this relation is preserved by means of restructuring – where necessary – of the original contract, *e.g.* by means of partial unwinding of the original deal.

Where a derivative contract hedging a specific position/item were to be eligible for clearing through CCP, then it would not be possible to proceed as described above (*i.e.* by a dynamic risk management of the positions), due to the fact that CCPs do not allow to unwind contracts/deals which are centrally cleared. The "common practice" applied for the management and the amendment of the characteristics and purpose of the original derivative contract for HA implies (i) the conclusion of a contract with identical features (to the original contract) but with 'opposite sign' (*i.e.* long vs short position and vice versa) and implies (ii) the conclusion of another new derivative contract with characteristics/features needed/desired. Following that, in occasion of the first 'compression', those two identical derivative contracts with 'opposite sign' would net off and only the other derivative contract with features/economic terms identical to the hedged balance sheet item would remain in place.

We are not sure that the practice just described above is considered compliant and acceptable by the International Accounting Standard Board (IASB), responsible for the definition of the relevant accounting international standards. In fact, banks and financial intermediaries would encounter serious issues with the dynamic risk management of the items identifiable as HA (not to mention the 'proliferation' of related derivative contracts, as described above) and this would make necessary the implementation of new procedures and traceability processes for the hedging contracts (for the 'hedged').

<ESMA_QUESTION_12>

Annex III - Impact assessment

Question 13: Please indicate your comments on the CBA.

<ESMA_QUESTION_13>

We have no comments on this topic.

<ESMA_QUESTION_13>