Deutsche Bank

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**Re: ESMA consultation on the Clearing obligation under EMIR for Credit Default Swaps (CDS)**

Dear Sir or Madam,

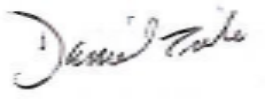
Deutsche Bank welcomes the opportunity to provide comments on the above consultation. We agree with the majority of ESMA's analysis and proposals. In particular we support the draft determinations on the classes of derivatives proposed for mandatory clearing and ESMA's intention to keep other CDS classes under review.

We support ESMA's proposal to split the frontloading window into two periods, A and B, to mitigate the challenges presented by frontloading. However we are concerned that, in order to minimise their frontloading obligations in Period B, category 2 counterparties (financials which are not clearing members) could be compelled to clear as soon as possible rather than benefitting fully from the 18 month phase-in. To avoid any adverse impact on the smooth implementation of mandatory clearing, we support restricting frontloading to category 1 counterparties (clearing members) by using the minimum remaining maturity (MRM) threshold to remove frontloading for category 2 counterparties.

The MRM for untranched index CDS trades in Period A should be increased to 4 years and 9 months. Five year contracts with a roll date of 20 September or 20 March, typically have a maturity of 5 years and 3 months. Therefore, despite ESMA's intention, frontloading may apply in Period A if the MRM is maintained as 4 years and 6 months.

Please do not hesitate to let us know if you have any questions about these points or if there are any issues related to this topic which you would like to discuss further.

Yours sincerely,



Daniel Trinder
Global Head of Regulatory Policy

## 1 The clearing obligation procedure

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

We agree with ESMA's approach.

## 2 Structure of the credit derivatives classes

**Question 2: Do you consider that the proposed structure for the untranched index CDS classes enables counterparties to identify which contracts are subject to the clearing obligation as well as allows international convergence? Please explain.**

We agree. For legal and operational certainty we recommend that ESMA clarifies that a CCP must be authorised and available to clear a class of derivative subject to a determination for the mandatory clearing obligation to apply.

## 3 Determination of the classes of OTC derivatives to be subject to the clearing obligation

**Question 3: 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 credit OTC derivatives?**

**Given the systemic risk associated to single name CDS, would you argue that they should be a priority for the first determination as well? Please include relevant data or information where applicable.**

We agree with the classes currently proposed for mandatory central clearing. As we support the objective of expanding clearing to all suitable classes, we also agree with ESMA's intention to monitor other CDS classes for potential inclusion in subsequent rounds of determinations on mandatory clearing.

## 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 4: Do you have any comment on the analysis presented in Section 4.1?**

We would agree with ESMA's analysis where ICE Clear Europe is authorised - as ESMA expects - by the time the RTS enters into force. Where ICE not authorised when the RTS enters into force and by the time mandatory clearing starts, this could create some confusion among counterparties and potential market disruption given ICE's important role in CDS clearing. Clarity would therefore be welcome on the approach that will be taken if ICE is not authorised by the time the RTS is due to enter into force.

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

**Question 5: Do you agree with the proposal to keep the same definition of the categories of counterparties for the credit and the interest rate asset classes? Please explain why and possible alternatives.**

We agree with ESMA's proposal.

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

**Question 6: Do you consider that the proposed dates of application ensure a smooth implementation of the clearing obligation? Please explain why and possible alternatives.**

The proposed phase-in of six months for category 1 counterparties is reasonable. Absent frontloading, the proposed 18 month phase-in for category 2 counterparties would in all likelihood be sufficient to ensure a smooth implementation of the clearing obligation. However, we are concerned that continuing uncertainty around how frontloading will work in practice will prevent the 18 month phase-in from being utilised fully and could compel category 2 counterparties to clear as early as possible so that they can minimise their frontloading obligations. This would be inconsistent with the objective of providing an 18 month phase-in to support the smooth implementation of the clearing obligation.

## 5 Remaining maturity and frontloading

**Question 7: Do you consider that the proposed approach on frontloading ensures that the uncertainty related to this requirement is sufficiently mitigated, while allowing a meaningful set of contracts to be captured? Please explain why and possible alternatives compatible with EMIR.**

We welcome the use of the minimum remaining maturity (MRM) threshold to mitigate frontloading in Period A. This has resolved most of the uncertainty around the frontloading requirements. We also agree with ESMA that non-financial counterparties should not be subject to frontloading requirements. However, we think that frontloading may result in category 2 counterparties being compelled to clear contracts as soon as possible and result in them not being able to benefit fully from the 18 month phase-in. This will occur as a result of pricing difficulties and legal and operational uncertainties that will still exist in Period B. While participants will know which contracts will be subject to the clearing obligation when entering into a contract during Period B, clients will not know whether they will in fact be able to clear the contract when the clearing obligation becomes effective or all the terms on which they will be able to clear the contract.

To address these uncertainties and provide category 2 counterparties with a phase-in period that can be utilised fully, we suggest setting the MRM of contracts entered into during the phase-in period (where at least one counterparty to the contract is a category 2 counterparty) using the approach proposed by ESMA for Period A, thus excluding category 2 counterparties from the frontloading requirement. Restricting frontloading to category 1 counterparties would maintain a degree of frontloading and be consistent with EMIR while scoping out category 2 counterparties which are often buy-side entities.

With the removal of frontloading for category 2 counterparties, a reduced phase-in period for these counterparties may be appropriate. However, sufficient time would still be required to ensure these counterparties are able to put in place clearing arrangements. A phase-in of less than 12 months is unlikely to be adequate. It would have to be sufficiently long to also allow counterparties apply for intra-group exemptions.

Further important points that should be considered include:

- The 5 year iTraxx main and cross-over indexes with a roll date in September 2014 will mature in December 2019 after 5 years and 3 months. If the MRM for Period A is set at 4 years and 6 months as currently proposed, a contract traded on these indexes during Period A may still be subject to the frontloading requirement despite ESMA's intentions. The proposed Period A MRM should therefore be changed for untranched index CDS trades to 4 year and 9 months;
- Period B should not start when the RTS is published in the EU Official Journal (OJ) as this date is not pre-defined. Period B should start at least 3 months after the RTS is published in the OJ in order to give market participants sufficient time to draw up legal agreements;
- It is important that the status of intra-group exemptions is clear before the RTS enters into force in order to give certainty on whether intra-group trades will need to be subject to the frontloading requirements.

## Annex I - Commission mandate to develop technical standards

## Annex II - Draft Regulatory Technical Standards on the Clearing Obligation

**Question 8: Please indicate your comments on the draft RTS other than those already made in the previous questions.**

It would be beneficial if ESMA provided clarity on the interaction between the IRS and CDS RTS. As currently drafted market participants have struggled to understand whether the two RTS will be adopted together, or whether the RTS in the CDS consultation paper, will supersede the RTS in the IRS consultation paper. It is also unclear what approach will be taken to any potential future proposal on extending the mandatory clearing obligation. Clarity on these issues is important as they impact how the phase-in and frontloading provisions are to be applied where they cover different types of product categories with differing starting dates for the clearing obligation.

The product classes listed in the tables in Annex I should be numbered in order to ease the reference for possible future Commission Delegated Regulations that may add additional product classes and specify new implementation periods.

## Annex III - Impact assessment

**Question 9: Please indicate your comments on the Impact Assessment.**

N.A.