



Association des Banques et Banquiers, Luxembourg
The Luxembourg Bankers' Association
Luxemburger Bankenvereinigung

Response from the ABBL to the Joint Discussion Paper 2012/1 on the Draft Technical Standards on risk mitigation techniques for OTC derivatives not cleared by a CCP under the Regulation on OTC derivatives, CCPs and Trade Repositories

Information about the ABBL:

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Capacity	Industry trade body
MS of establishment	Luxembourg
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Introduction

As in its responses to ESMA and EBA, the ABBL¹ would like to first of all invite the 3 agencies to take all the reasonable time available to prepare technical measures of quality even if the association understands that the EU authorities are under extreme pressure to complete the regulatory process in due time to meet the G20 agenda.

Although this paper is of good quality, the ABBL strongly regrets that so little time has been dedicated to seek stakeholders' views on such important documents. Responding to 3 different consultations on the same subject within a month and without a final text, only agreed on the 26th of March, is extremely difficult. It appears even counterproductive as regards the aim of increasing systemic resilience of the EU market infrastructures.

Priorities

The ABBL will thus concentrate its contribution on some elements that it considers of priority. As rightly pointed out in the document EMIR is born out of a G20 requirement. One of the priorities should then be to align to the maximum extent the rules across the globe. Thus, the association is pleased to see that a specific emphasis will be put on IOSCO or Basel Committees rules and proposals.

The association considers that one of the inherent features of a dual approach to margins (IM+ VM) is that they follow the market trends. They thus would have a natural tendency to be cyclical. It may be a second step to view them as pro-cyclical with the idea that the riskier the environment the higher the

¹ The Luxembourg Bankers' Association (ABBL) is the professional organisation representing the majority of banks and other financial intermediaries established in Luxembourg. Its purpose lies in defending and fostering the professional interests of its members. As such, it acts as the voice of the whole sector on various matters in both national and international organisations.

The ABBL counts amongst its members' universal banks, covered bonds issuing banks, public banks, other professionals of the financial sector (PSF), financial service providers and ancillary service providers to the financial industry.

margin. The association is not convinced that introducing counter-cyclical buffer is a sound idea given the nature of the participants in the market, who are either long term users, corporates or PRFCs.

The ABBL sees some value in a mixed approach, whereby an initial margin is set so that it covers normal trading activity, the variation margin shall be triggered only when the price of the underlying deviates substantially from their “original” pattern. The objective would be to limit back and forth wires of funds from the “client” to the financial institution. This creates a procedural burden that is of limited interest without the potential reduction of systemic failure that may justify such an option. The table on page 12 should be reviewed to replace “only VM” by “only IM”, since the association considers the IM as the preferred option to prevent systemic risk and reduce pro-cyclical effect.

Regarding the eligible collateral, the association is of the view that it is surely preferable at this stage that the scope or type of instruments eligible are wide, but that appropriate haircuts should be imposed on the different assets. Regulators should keep in mind that the entities in the scope of this discussion paper are not only financial institutions but may be non-financial organisations. Collateral will be scarce for all institutions, even more so when they are non-financial institutions. The aim of EMIR is to improve markets, economic stability and reliability; it should not be to exclude many players from their markets. The proposal not to rely only on CRA/ECAI may thus be an incentive to broaden the scope of instruments eligible for margin/collateral.

The association invites the ESAs to keep in mind that the nature of clients envisaged here is very diverse. It may include the PRFCs for tailored contracts, but a lot of activity will come from NPRFCs or NFCs that represent probably a more diverse biotope. This means increased possibilities to spread risk over parties with diverging interests rather than among a group of different but otherwise similar institutions as is the case among the PRFC community.

The framework should probably envisage a regulation “above the threshold”, but leave open the possibility for PRFCs to require collateral from any participant. Regarding the 3 scenarios envisaged for the posting of collateral, the association considers that option 1 is probably the most transparent but the least flexible for clients. A combination of option 2 and 3 should then be the optimal outcome, especially considering the fact that this discussion paper is complementary to the requirement in case of on CCP clearing. Criteria to collect collateral or not should be adapted by the PRFC depending on its counterparty and the market evolution, but fixed default criteria may be required.

Regarding variation margin the paper shall clarify what happens when market conditions are so accommodative that the risk level creates a negative VM that leads to a valuation below the IM.

In answer to question 16, the association would tend to say that although it may be possible and positive for PRFCs to rely on internal models to compute risks, when it is in interaction with NFCs it may be more transparent and simpler to use a standardised approach. The issue here is notably to take into account the fact that entities subject to EMIR should be subject to a global framework and they may opt for a regulatory arbitrage outside of the EU if they are offered a much better treatment.

In the list regarding the re-use of collateral and segregation the association considers that this should be contractually driven. The segregation of cash is, for example, contradictory with accounting principles. Ideally, segregation of assets from the PRFC and its clients should be the norm. Cash may be deposited in a money market fund of prime quality so that it falls under the segregation rules of financial instruments.

Regarding intragroup transactions reference can maybe be found in the CRD/CRR regulation.