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The Bank of New York Mellon – London Branch

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The Bank of New York Mellon's comments on the ESMA Discussion Paper - Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories

Introduction

BNY Mellon is grateful for the opportunity to provide responses to the questions raised in the European Securities and Markets Authority's (ESMA's) Discussion Paper entitled "Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories" (the Discussion Paper) dated 16th February 2012. Our responses to the questions raised in the Draft Discussion Paper are set out below: we provide responses to queries with particular relevance to our asset management and asset servicing clients, who themselves invest in a wide variety of derivative instruments, as well as to our activities as a large bank counterparty engaging in foreign exchange activities of importance to financial markets.

BNY Mellon appreciates the scope and pace of Regulation and, despite its importance, recommends that ESMA consider carefully the timeline for implementation in view of the difficult operational and legal challenges posed by the Regulation.

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About The Bank of New York Mellon

The Bank of New York Mellon (BNY Mellon), founded in 1784, is a multi-faceted financial holding company providing banking and investment and asset services globally. Headquartered in New York, BNY Mellon has approximately \$25.9 trillion in assets under custody or administration – making it one of the largest global custodians active in settlement, payment and financial market services activity throughout the world - and \$1.2 trillion in assets under management on behalf of underlying clients. BNY Mellon is located in 36 countries and services over 100 markets worldwide.

The goals envisaged with the implementation of EMIR are strongly supported by BNY Mellon. BNY Mellon has actively supported and participated in many efforts to reduce systemic risk since its founding. BNY Mellon was one of the founding members of the New York Clearing House Association in 1853, which provided a mechanism for banks to settle their daily accounts with each other in a single secure location and which provided a line of defence against shocks to the system during times of financial crisis.

Responses to Queries in the Discussion Paper

I. OTC Derivatives

1. Contracts between third country entities having an effect within the EU

Q1: In your views, how should ESMA specify contracts that are considered to have a direct, substantial and foreseeable effect within the EU?

Determination of specified contracts should be phased in over time, with individual types of contracts being specified rather than products that might have a “direct, substantial and foreseeable effect within the EU.” The criteria of notional market size (compared to average market size), type, location and expertise of counterparties, as well as the length of the contract or the underlying, should all be taken into account where they deviate substantially from conventional trades. The nominal currency or that of an underlying could be a proxy for a substantial effect within the EU.

The obligations of a clearing party to the CCP when the clearing party enters into trades with third country entities should be clarified: an example requiring clarification would be an OTC

derivative that has been concluded between an EU counterparty to an OTC derivative and a third country entity having its own clearing obligations.

In order to avoid highly disruptive confusion and uncertainty among market participants and prudential regulators, conflicts and inconsistencies should be prevented among different – sometimes overlapping - sets of legislation (e.g. EMIR/Dodd-Frank): for example, a transaction could be required to be cleared and reported in more than one place. More fundamentally, the scope of the clearing obligation needs to be decided upon and implemented consistently across different legal and regulatory regimes. There is a crucial need for harmonisation with other legislation such as Dodd-Frank so that there is definitional convergence and consistency regarding the scope of the clearing obligation. Otherwise, other relevant legislation (such as Dodd-Frank) may apply to the same contracts in different ways such that under EMIR the clearing obligation may apply whilst under Dodd-Frank it might not. An example is in the context of foreign exchange: whilst the U.S. Treasury has proposed an exemption from Dodd-Frank swap clearing and trading requirements for foreign exchange “swaps and forwards” within certain parameters in recognition of – among other things - the extent to which settlement risk has been adequately addressed via mechanisms such as CLS, which has significantly reduced systemic risk (i.e., “Herstatt Risk”). There is no indication that such an exemption would apply under EMIR. Instead, it is proposed that ESMA would have authority to exempt FX transactions from the clearing requirement, which would create undue uncertainty for bank and other trading desks which tend to operate on a global basis – often through branch structures - in order to cover continuous trading requirements over the global trading day. As things stand today, it is possible the scope of transactions potentially subject to mandatory clearing may differ between the U.S. and the EU.

Q2: In your views, how should ESMA specify cases where it is necessary or appropriate to prevent the evasion of any provision of EMIR for contracts entered into between counterparties located in a third country?

ESMA is unlikely to be in a position to effectively supervise third country counterparties. Instead, ESMA should focus on determining whether adequately similar rules are in place in relevant third countries, with guarantees to ESMA of sufficient access to the information.

It should be clarified that if the EU and other jurisdictions implement varying approaches regarding the same types of contracts, this in itself should not be seen to give rise to “evasion”. The example described in the response to Question 1 above provides is relevant in

this respect: it would be highly disruptive if foreign exchange contracts entered into in Tokyo, Singapore or New York, which are expected to be considered bilateral in nature and outside the scope of the mandatory clearing and other obligations, are subjected to “cherry-picking” by ESMA and thus undoing the benefits of scale and existing operational and legal clarity in these markets. It is recommended that ESMA seek to harmonise its approach with other jurisdictions – where sensible - in order to minimise disruption to markets and other risk-reduction mechanisms that are successfully operating elsewhere. This approach may take the form of blanket exemptions (where appropriate) or recognition of “equivalent effect” in third-countries.

2. Indirect Clearing Arrangements

Q3: In your views, what should be the characteristics of these indirect contractual arrangements?

BNY Mellon welcomes guidance from ESMA regarding indirect arrangements and welcomes the opportunity for market actors to use indirect clearing arrangements between counterparties/clients and clearing members. Rather than specifying particular types of arrangements, or prescribing standards for them, it would be preferable for ESMA to specify criteria these arrangements should meet. As an example, indirect clearing arrangements might include when a client clears transactions for its own client. The client of the clearing member would be an agent for its own client.

However, with EMIR taking effect on the 1 January 2013, there will be significant challenges for at least smaller and medium-sized entities. These entities would in most cases have to find a clearing member or a client of a clearing member that is willing to provide access to the CCP to them.

There are currently no standard indirect clearing arrangements and in view of the fact that these will have to be adjusted to the requirements of all CCPs, it is unlikely that a single standard can be developed. Thus, the contractual arrangements between clearing members and clients as well as between clients of clearing members and their clients would need to be negotiated. The approach generally would be based on existing standardised master agreements, however, the arrangement would need to be adapted in order to address a number of complex CCP-Clearing-related issues as well as complex legal issues such as principles of

agency versus principal in order to ensure legal recognition of indirect arrangements (which would be crucial in the insolvency setting).

The negotiation of such arrangement will therefore be very time consuming and can only be finalised if all relevant details concerning the applicable regulatory framework as well as the requirements of the relevant CCPs are known. Comments of some members suggest that the preparation of contracts between medium sized banks and clearing members regarding indirect clearing access (due to the lack of standardisation in this field) are estimated to take about 5 to 6 months. If connections to two clearing members are compulsory and taking into account that the relevant standards that will supply at least part of the framework requirements for the design of these contracts are not released yet, there is a justified fear among some stakeholders that it is already very late in the day to start searching for counterparties if a financial wants to adhere to EMIR starting on 1 January 2013. Consequently, we believe that there has to be a phase-in period. This issue could be addressed in connection with the phasing-in of the clearing-obligation in respect of certain class of derivatives.

In this connection, market participants currently already rely on various types of standardised contractual documentations (master agreements), including the ISDA Master Agreements, the European Master Agreement, the German Master Agreement for Financial Derivative Transactions and the French Master Agreement. These forms are generally accepted and/or recommended by trading or industry organisations and are put through rigorous legal reviews, usually subjected to legal opinions capable of being tested in times of financial crisis and insolvency. As a result of their high level of standardisation and as they address key legal and insolvency issues, especially close-out netting, they are an important element for mitigating legal and counterparty risks.

Indirect clearing arrangements could therefore be based on these master agreements. The requirements should however not mandate the use of one specific type of master agreement. Rather, market participants must continue to be able to choose to select the best master agreements in their own judgments, including the applicable law best suited to their needs and operational capabilities. Moreover, it should be recognised that even the ISDA and similar form agreements which might be used to establish legally effective “indirect” relationships will require significant legal review of relevant applicable law in order to ensure

certainty. It is possible multi-jurisdictional legal opinions may be required, which would be a very significant undertaking: as indicated above, this would be especially crucial in insolvency situations.

The contractual framework would need to be sufficiently transparent and also operationally manageable for all counterparties. Non-financial counterparties in particular may have difficulties dealing with the complexity of the contemplated contractual arrangements, even more so where such arrangements cross jurisdictional boundaries. The goal of identical protection among widely divergent types of ultimate investors - and regardless of whether they are contracting directly or indirectly – will be a very demanding project which would need to be completed in a very short period of time.

3. Implementation of the clearing obligation

Q4: What are your views on the required information? Do you have specific recommendations of specific information useful for any of the criteria? Would you recommend considering other information?

Some of the information, e.g. tightness of spreads, is not likely to be readily available.

A major issue confronting ESMA is that even within a seemingly similar class of derivatives, there may be several important differences, including dates, sizes, or agreed governing law. Any agreements prescribed by ESMA should seek to standardise contract parameters. For example, certain terms of contracts could become standardised, such as duration (which could be standardised at 10, 30, 90 days, etc.) or minimal notional amount (which could only be sensibly done by contract “type”). Most of information required by ESMA would be available at the Trade Repository, except information relating to pricing / liquidity (this information will be very difficult to obtain as, due to the nature of these products, there is no market price). In these conditions, it would be appropriate to require a certain minimum track record in the Trade Repository prior to deciding if a particular OTC derivative should be eligible for the clearing obligation.

BNY Mellon recommends explicit reference in the criteria to ESMA’s determination as to operational readiness of counterparties (and their agents) in moving to central clearing of a contract. Whilst the competent authority of the relevant CCP is obliged to provide information on readiness, this will not necessarily reflect the actual market position: a

determination by ESMA would provide for the necessary public disclosure regarding operational, legal and risk management readiness of counterparties (and their agents).

BNY Mellon would also welcome clarification regarding the use of public consultations and timeframes within which they would be conducted. It appears that public consultations prior to drafting technical standards would only be mandated where ESMA follows a “top-down” approach and not explicitly in the case of notification from a competent authority. BNY Mellon would advocate public consultation regardless of the initiation method.

Q5: For a reasonable assessment by ESMA on the basis of the information provided in the notification, what period of time should historical data cover?

This factor is dependent on the type of product and the maturity of the product class. It should cover a reasonable period, so that enough market environments have been experienced to test liquidity, market activity; a minimum duration of 12 to 36 months is sensible. For new products, prospective assessment can only be conducted by utilising a proxy and estimation. A period of 6 to 12 months should elapse during which performance can be matched against these estimates and proxies.

A phasing-in process should be adopted as well.

Q6: What are your views on the review process following a negative assessment?

The fact that ESMA arrived at a negative assessment should be made public. There should be a minimum waiting period of at least one year following a negative assessment for resubmission of a notification. This not only would mitigate the workload of ESMA, but it would also regularise and make predictable the considerable administrative processes associated with a new assessment by all market participants. Market participants will generally need to begin with their implementation processes immediately after becoming aware of the fact that the introduction of CCP-clearing for a new class of derivatives is under review.

Without an adequate minimum waiting period, market participants would be faced with the clearly unreasonable prospect of permanent preparations for a new CCP-clearing obligation.

Q7: What are your views regarding the specifications for assessing standardisation, volume and liquidity, availability of pricing information?

- Standardisation of contractual documentation (item 22 a.)

One key element should be the use of contractual terms contained in or corresponding to those used in master agreements (please see response above to Q 3).

- Proportionality of margins and historical stability of liquidity (item 22 b.)

Even if instruments appear to be liquid at one point in time they may experience distortions under different market conditions. This strengthens the case for having a relatively long period of assessment.

- Accessibility of pricing information (item 22 c.)

CCP clearing is only possible with a sufficient degree of liquidity / sufficiently high trade volume. The thresholds to be set in this respect should therefore have a sufficient safety margin.

- Liquidity considerations are crucial. ESMA should confirm its plans for assessing liquidity as it evaluates clearing eligibility. Liquidity is referenced in many other regulations (e.g., MiFIR, CRD IV), but the market still lacks a clear and common understanding.
- It should be recognised that the mere existence of a clearing obligation may impact future liquidity of the contracts. Clearing may not necessarily increase liquidity in the market, and there may be circumstances when liquidity could in fact decrease following a mandatory clearing obligation. An example of this may arise where two classes of derivatives are traded “together” with the intention of providing for naturally occurring offsetting behaviours: however, only one of those classes of derivatives may be liquid enough to be able to be cleared, resulting in one but not the other derivative transaction being subjected by ESMA to the mandatory clearing obligation. This could lead to a bifurcation of positions, with some being cleared and others being risk-managed on a bilateral basis. This not only would increase counterparty risk (since the independent offsetting of the positions would no longer naturally occur), but it may also lead to a reduction in liquidity of certain classes of derivatives (even those that are cleared). As a consequence of this concern, in determining the criteria for the mandatory clearing obligation, ESMA may wish to consider 1) the potential downside of such an obligation;

and 2) if phasing in of the clearing obligation can be introduced by category of counterparties – rather than of instruments - in order to limit these kinds of consequential risks.

- It should be recognised that in some cases, a mandatory clearing obligation could increase other risks to market participants or lead to other unintended consequences. These might include, but not be limited to, an increase in repurchase and other financing transactions (thereby increasing counterparty credit risk) in the market as a result of market participants needing to transform physical collateral into cash in order to meet cash variation margin obligations for clearing. ESMA should ensure that the benefits of applying mandatory clearing obligation for a particular class of derivatives outweigh the risks of any unintended consequences.
- The number of transactions is connected with liquidity, but ESMA (and EMIR) are right to differentiate between the two concepts. While not being in a position to pinpoint a minimum threshold for liquidity we believe that 100 transactions a day should be the lowest limit for the number of transactions.
- It is very important to take into consideration the differences in liquidity/volume by currency. For example the liquidity in NOK IR Swaps may be insufficient for CCP-clearing, whereas liquidity in EUR IR Swaps may be sufficient.
- When assessing the classes of transactions to be subject to the clearing obligation consideration needs to be taken to the fact that there are transactions that are made within such classes which are not suitable for clearing, or even possible to be cleared. One such example are derivative transactions, such as interest rate swaps made for covered bonds (or the cover pools), which on the surface may be standard products but which, due to requirements under applicable law and regulation, have terms and conditions which will not be compatible with the clearing system (e.g., one-way collateral, no possibility to terminate in case of bankruptcy of the bank, etc.). As such, covered bond issuers should not be subject to the clearing obligation when it comes to derivatives that (with reference to the above) do not fit neatly into the clearing system. An issuer of covered bonds may not place collateral due to legal impediments concerning the position of the party to a derivatives contract in ranking. The obligation for CCP-clearing would cause double treatment and thus a standardisation based on instruments would not work.

- Finally, EMSA should consider requiring a formal process to be put in place where a mandatory clearing obligation on a particular class of derivatives could be revoked upon a change in market conditions, which could cause the clearing obligation criteria set out by ESMA to no longer be satisfied for such a class of derivatives.

Q8: What are your views, regarding the details to be included in ESMA Register of classes of derivatives subject to the clearing obligation (Article 4b)?

To avoid uncertainties and confusion, the term “currency” used in item 24 d. should be replaced by “settlement currency”.

Q9: Do you consider that the data above sufficiently identify a class of derivatives subject to the clearing obligation and the CCPs authorised or recognised to clear the classes of derivatives subject to the clearing obligation?

We have no comments regarding the information required for the identification of the CCPs. As for the details regarding the timeline for the entry into force of the clearing obligation, we note that item 26 only mentions phasing-in in relation to types of counterparties. This should, however, also provide for a step-by-step phasing-in based on criteria other than the counterparty (e.g., with reference to sub-classes of products or threshold amounts) in order to allow a more structured and predictable initiation of clearing for a product class.

BNY Mellon welcomes the establishment of an LEI, because it would allow for a most efficient and unambiguous identification. However, the use of the LEI should not lead to changes in the application of local law rules (e.g., if a subsidiary uses the same LEI as its parent, the former could be forced to apply rules that are different from the country where it is located, and correspondingly, some other entities might be unduly favoured).

4. Non-Financial Counterparties

Q10: In your view, does the above definition appropriately capture the derivative contracts that are objectively measurable as reducing risk directly related to the commercial or treasury financing activity?

A possible unintended consequence may arise due to the way the exemption for non-financials lines up with the temporary pension scheme exemption. Since pension schemes are still considered financial counterparties, non-financials (who would be exempt in the case of commercial hedges and non-hedges falling under the clearing threshold) will be

incentivised to retain liabilities on their balance sheets once the pension scheme exemption expires. Prudent approaches to balance sheet management may be disincentivised.

Q11: In your views, do the above considerations allow an appropriate setting of the clearing threshold or should other criteria be considered? In particular, do you agree that the broad definition of the activity directly reducing commercial risks or treasury financing activity balances a clearing threshold set at a low level?

The obligation to determine qualification should remain exclusively with the non-financial – and a financial counterparty should be able to rely on this conclusively: financial counterparties would have no means of independently verifying qualification of the non-financial counterparty.

In the interest of legal certainty, the fact that a specific non-financial entity has become subject to the clearing obligation needs to be notified to all potential counterparties and/or to the public, e.g., by listing the identity (if possible by LEI) of the relevant non-financial entities in the register maintained by ESMA. If an entity is not listed in that register no counterparty should be held responsible for not centrally clearing a transaction with this non-listed counterparty. Counterparties are not in any position to determine whether the thresholds are met or not and cannot be expected to decide whether a non-financial counterparty is subject to the clearing obligation or not. This would become especially difficult in the context of third country counterparties since there will be no way to ensure that such counterparties provide the necessary information.

BNY Mellon agrees that it is sensible to distinguish between thresholds applicable to individual legal entities versus the group, however, it crucial to keep in mind that clearing arrangements need to be done on a legal entity basis. Consequently, the regulation should not require all legal entities in the group to clear once a group-level threshold is exceeded. To require otherwise would likely incentivise avoidance. Other potential problems arising from group-level thresholds might include where entities in the group are located outside the EU, or where the group is headquartered outside the EU.

5. Risk mitigation for bilateral transactions

Q12: What are your views regarding the timing for the confirmation and the differentiating criteria? Is a transaction that is electronically executed, electronically processed or electronically confirmed generally able to be confirmed more quickly than one that is not?

Generally, BNY Mellon is concerned about prescribing inflexible rules with respect to timing of confirmations given the range of practice across different kinds of counterparties, different asset classes and the varying systems capabilities of market participants.

The discussion paper distinguishes between non-financial counterparties exceeding the clearing threshold and those that do not, although it is unclear why this distinction is justified or which time periods would apply where one party is a financial counterparty and the other a non-financial counterparty not exceeding the clearing threshold.

It is also unclear whether both sides to a trade should be required to confirm within the prescribed time limits. We assume this is not intended in a dealer/client relationship, where the dealer is typically responsible for producing the confirmation and the client then has a certain time period in which to affirm or reject the trade. We would encourage the obligation to be solely on the executing dealer to initiate the production of the confirmation within prescribed time periods but not the affirmation/acceptance of that confirmation by the end client.

The proposed time limits also fail to factor in the allocation of block trades. Whilst asset managers (for example) trading for a number of underlying clients will typically allocate on the same day, it is unrealistic to allocate within the suggested time limits, resulting in a delay to the confirmation initiation process.

The time in which confirmations can be readily produced is likely to vary significantly by asset class and the extent to which bespoke arrangements are put in place between the parties. The more bespoke the arrangement, the longer it takes to produce and agree a confirmation which will typically involve legal discussions between the parties.

More specifically:

- Definition/scope of the confirmation: Information to be included should be clearly prescribed. Current practice and market practice is that confirmations cover the key terms of the transaction and do not act as a substitute for underlying legal documentation. It should also be clarified that the time limits to be defined by the technical standards apply to the initiation of the confirmation process, i.e., the first transmission of the confirmation by one of the counterparties and not the receipt of a countersigned-confirmation/affirmation/acknowledgment by the other counterparty or the matching.
- Electronic- and non-electronic confirmation: BNY Mellon encourages ESMA to clarify the timeline for implementation of electronically executed and processed confirmation. The time required for an electronic confirmation can vary considerably depending on the type of transaction and market participants involved. For example, confirmations concerning bulk transactions are significantly more time consuming than confirmations of single simple transactions. Likewise, less sophisticated market participants (which would include a significant portion of market participants falling under the definition of financial counterparty) will have a significantly less developed infrastructure for the processing of transactions and thus will generally require more time for processing transactions. Consequently, the benchmarks set by highly sophisticated market participants and in relation to simpler transactions should not establish the standard for all electronic confirmations.
- Proposed time limits for timely confirmation (items 38 a. to c.): The time limits proposed under item 38 a. to c. appear to be based on benchmarks set by highly sophisticated market participants - and in relation to simple transactions - and thus cannot be applied to all market participants or to all transaction types. The timeframe for confirmation of transactions not executed electronically should – if meant to apply comprehensively – be extended. Many OTC derivatives transactions undertaken for hedging purposes still confirmed via fax or post. The proposed timelines will require significant changes to IT systems both among financial institutions and non-financial institutions: a distinction between transactions involving financial counterparties and non-financial counterparties exceeding the threshold on the one hand and non-financial counterparties not exceeding the threshold on the other hand is not necessary or helpful in this context. The following

limits would be more realistic and ensure a higher quality and efficiency of the confirmation process:

- Electronic execution/electronic processing: 24 hours
- Non-electronic processing/execution: 120 hours (= 5 days)

Should the technical standards also set out timelines for the receipt of the countersigned confirmation by the other party, the timelines will then need to be correspondingly longer (in any event not less than two weeks).

Q13: What period of time should we consider for reporting unconfirmed OTC derivatives to the competent authorities?

- Definition/meaning of outstanding/unconfirmed:

The terms outstanding and/or unconfirmed transactions need to be clearly defined and differentiated. Not all transactions which are not confirmed should be considered “outstanding”.

We suggest the following definitions:

- Outstanding transactions: Encompasses unconfirmed transactions as well as confirmed transactions for which the reporting party has not yet received a (counter) confirmation from the counterparty and/or which have not yet been matched/ executed.
- Unconfirmed transactions: From the perspective of the reporting entity, transactions for which no trade confirmation has been issued by the relevant party and/or received from the counterparty.

- Timeline for reporting:

A period of more than 30 days would be appropriate. However, market participants should be permitted to make the reports in batches (once per month). The relevant reports should be made once per month in respect of unconfirmed transactions in the preceding month

Adequate timelines would increase the efficiency of the processes and the accuracy of the data.

Q14: In your views, is the definition of market conditions preventing marking-to market complete? How should European accounting rules be used for this purpose?

Whilst BNY Mellon largely supports ESMA setting out guidance and rules on when mark-to-model or mark-to-market should be applied, ESMA should not attempt to prescribe how a mark-to-market or mark-to-model would be constructed. Market participants must be provided with sufficient flexibility to be able to develop best practices and methodologies for pricing and valuing positions.

The definitions of mark-to-market and mark-to-model also need to be flexible. There are many classes of derivatives that may have elements of both models. For example, some classes of derivatives contracts utilise pricing parameters that are widely quoted in the market (such as implied volatility in the pricing of options contracts) but actual pricing requires feeding these quoted parameters into a model. Any rules regarding mark-to-market or mark-to-model should not prohibit market participants from being able to value the contracts in the manner that best captures fair value of the contracts based on industry best practice.

Market inactivity should be defined both in terms of transaction per time unit and also in terms of tradable size. References to the lack of similar contracts and the nature and complexity of the derivative should be reasons to use mark to model. In 45.a. the notion of “all factors” is always subject to caution. BNY Mellon would prefer wording based on “all useful” or “most relevant factors”.

It should be recognised that exhaustive prescription may be not be possible to implement in practice.

Q15: Do you think additional criteria for marking-to-model should be added?

We believe that marking-to-model valuation technique should not be regulated in the CCP regulation as it is already prescribed elsewhere, such as by IFRS. Further, individual risk valuation techniques should not be required to be taken to the board for approval. The board

is responsible for the firm having effective procedures for risk assessment but not for considering individual risk valuation techniques at board meetings.

Q16: What are your views regarding the frequency of the reconciliation? What should be the size of the portfolio for each reconciliation frequency?

Is unclear what would be considered sufficient reconciliation of non-cleared OTC derivative contracts. BNY Mellon considers that it is sufficient that a financial counterparty delivers a list of outstanding trades regularly to non-financial counterparty.

The suggested threshold for daily portfolio reconciliations under item 48 b. (300 transactions) is far too low. Effective and efficient reconciliations require a significantly higher number of transactions. The threshold for an obligation should therefore be set at not less than 5000 transactions as proposed for higher margin periods of risk in CRR 2 para 2 .

The thresholds and time limits proposed under item 48 b. would need to adjusted accordingly. It should be clarified whether portfolio reconciliation includes also reconciliation of collateral posted in respect of relevant portfolios.

Q17: What are your views regarding the threshold to mandate portfolio compression and the frequency for performing portfolio compression?

Portfolio compression can only be effective with a sufficiently large transaction basis. It also requires a highly complex and sophisticated infrastructure (internal as well as external) which can only be merited if the counterparty has a sufficiently large volume.

To ensure sufficiently effective and efficient portfolio compression and avoid unreasonable demands for market participants with small volumes, the transaction threshold needs to be raised significantly (to not less than 10000 transactions). Likewise, the frequency (twice per year) is not suitable or feasible in all circumstances and not in respect of all portfolios. Parties should not be required to take part in every single compression process.

It should be recognized that portfolio compression may not be equally relevant to all types of market participants. Asset management clients, for example, typically hedge risks in a single direction as opposed to having naturally offsetting trades. In addition to a threshold, it may

also be appropriate for ESMA to consider which market participants should be subject to compression by reference to the kinds of positions that they actively trade.

ESMA's current recommendations also do not appear to recognise that a single underlying client's portfolio may be diversified over multiple asset managers acting as that client's agent. Whilst a client may breach the compression threshold in aggregate, this will not necessarily be the case per manager, in which circumstances compression would not be appropriate.

Finally, trade compression is only relevant for standardised contracts (e.g. CDS). So it is surprising that ESMA makes reference to the portfolio compression for bilateral contracts which are not cleared through a CCP.

Q18: What are your views regarding the procedure counterparties shall have in place for resolving disputes?

The requirements will affect internal/operational processes as well as the contractual/legal framework (in particular issues addressed under item 54.c). When defining requirements regarding the legal/contractual framework for dispute resolution mechanisms, the focus should not be on the level of detail of such mechanisms but rather on the efficiency and (legal) effectiveness of the provisions that would govern the dispute. The master agreement regimes (described above) already provide for effective dispute resolution mechanisms, which have generally proven to be very effective.

The proposed timeframe (5 days) is too rigid and does not take into account the need for more time to resolve more complex disputes. We support the ISDA draft Convention on Portfolio Reconciliation and the Investigation of Disputed Margin Calls and Formal Market Polling Procedure (the "Draft DR Rules") as a basis of industry-endorsed methodology for resolving collateral disputes.

Finally, we recommend confirmation that any information on a dispute that is reported to competent authorities be treated as sensitive and confidentially. Collateral disputes could involve important pricing information and it may not be in the best interest of end investors to disclose this information to the counterparty in question or other counterparties.

Q19: Do you consider that legal settlement, third party arbitration and/or a market polling mechanism are sufficient to manage disputes?

Our answer depends on how flexibly these terms are employed: they should not preclude alternative dispute resolution mechanisms such as arbitration. The DR Rules (referenced in our response to the previous question) would present another alternative that should be permitted.

Q20: What are your views regarding the thresholds to report a dispute to the competent authority?

It is important to ensure a common understanding of what would constitute a dispute for the purposes of the relevant thresholds. Some concept of materiality should be adopted.

The time thresholds need to be sufficiently long to prevent hasty resolution that may be counterproductive (e.g., creating unpredictability and thus legal uncertainty). BNY Mellon proposes that the thresholds should be raised to at least 1 month/30m EUR. This would help the authorities to focus on the potentially serious/relevant developments.

BNY Mellon is concerned that information on the existence of disputes - especially the details - are highly sensitive and need to be treated as highly confidential: under no circumstances should they be made public.

Q21: In your views, what are the details of the intragroup transactions that should be included in the notifications to the competent authority?

Such counterparties should be required to notify competent authorities:

- (a) name;
- (b) name of the other counterparty with whom they wish to deal;
- (c) a description of the kind of transaction with respect to which they intend to take advantage of the exemption; and
- (d) a description of the risk management procedures that would be applied to the transaction(s); and
- (e) a statement that they meet the criteria established by the relevant ESA(s) in order to permit the transfer of own funds or repayment of liabilities between the counterparties.

This information may be sensitive or highly confidential (as it would reveal important information about the group's risk positions) and so should be protected and kept confidential.

Q22: In your views what details of the intragroup transactions should be included in the information to be publicly disclosed by counterparty of exempted intragroup transactions?

BNY Mellon believes that only name/identity of the entities in question should be disclosed. We also strongly believe that notifications should only be made once in respect of each entity falling under the exception and are not to be repeated on the occasion of each transaction. Any obligation to disclose information on the individual transactions made by the entities covered by the exception would raise serious concerns: For one, there is no discernible need for such information. Intragroup transactions fall under the reporting obligation and thus details of the transactions will be reported to trade repositories (TRs). The relevant information can therefore be accessed by the competent regulatory authorities and the information disclosed by the TRs in aggregate form to the public will therefore also cover these transactions. In view of the existing TR reporting requirement, it would also be clearly unreasonable to demand an additional/further disclosure of information on transactions, especially in view of the highly sensitive nature of the information in question.

Multiple or parallel (or even more than that) notification requirements to different entities must be avoided (see also question 69) and it should be permissible that the relevant notifications are made by one group entity on behalf of other group entities.

BNY Mellon would like to stress the need to have the official regulatory text published as soon as possible, to be able to fully consider these standards.