

DIA response to ESMA's Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade repositories

The Danish Insurance Association (DIA) welcomes the opportunity to respond to the Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories published by ESMA on 25 June 2012.

General remarks

The DIA agrees with the overall aim of the EMIR regulation including level 2 and 3 regulation to ensure healthier and more robust financial markets.

However, it is important to achieve the right balance (calibration) of EMIR in order to avoid unintended consequences for insurers such as a substantial reduction of hedging levels. This would – contrary to the intentions of EMIR - increase the overall risk for policyholders rather than reduce it.

Achieving the right balance depends in particular on the specific requirements in the level 2 and 3 regulation. In the present consultation, we have concerns with particular elements of the draft standards (e.g. indirect clients, transparency in pricing of the CCP, collateral), which are described in further detail in the specific remarks below.

Considering the quite substantive changes that have been presented so far in all the level 3 consultations, we find that it will be imperative that market participants are allowed enough time to adapt to the changes. This applies both in relation to the clearing obligation and in relation to the risk mitigating measures required for non-cleared derivatives. The changes intended seem to require substantial changes of the ISDA framework and will therefore imply renegotiations with many counterparties. Since contracts are often complex, renegotiation is a lengthy process. Further, queues may be created at those relatively few counterparties that at present seems to be able to be ready by the end of the year for membership of a CCP.

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Specific remarks

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Rights and risks of indirect clients

Even though the draft standard in Annex II is aiming to ensure the same protection of indirect clients as for direct clients, we believe that there will be increased risks (both legal and operational) associated with being an indirect clearing client. It is not clear to us what will be the economic consequences of these risks? Will the direct client be able to charge additional collateral from the indirect client who wishes to clear OTC Derivatives with the direct client? In that case it may be particularly expensive for the smaller insurers to clear OTC derivatives.

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Transparency in pricing of the CCP

The size of the initial margin seems – according to the estimates by market participants so far – to be of a substantial amount. However, the estimates on the initial margin also vary to a large extent. Considering the effect that this may have for insurers subject to the clearing obligation (and possibly also for those derivatives that are not subject to the clearing obligation) – and the fact that cost are calculated as a percentage of the initial margin – we believe that transparency regarding the calculation of the initial margin is of the utmost importance.

We have noticed that it is ESMA's view that the draft RTS should not require the disclosure of commercially sensitive information or information that would lead CCPs to competitive disadvantages, cf. paragraph 144, page 27. We urge that this possibility is eliminated or alternatively rephrased in a more narrow way but at least so that the direct client and the indirect client is able to calculate the initial margin and cost.

Collateral

We find it important and reasonable that Danish government bonds as well as Danish mortgage bonds due to their quality can be used as collateral for a CCP. Having read the draft standards, we assume this is the case.

Portfolio reconciliation, Portfolio compression and dispute resolution

We think that the intentions with the provisions on portfolio reconciliation and compression are good and reflects a sensible best practise. In particular we find the provisions on dispute resolution to be quite sensible. However, we do not see the need for a requirement to terminate the transactions that can be netted as required in Article 3 RM, nr. 3, page 74.

Phasing-in of the clearing obligation

In article 1 DET,2 a possibility for the CCP of phasing-in the clearing obligation by counterparty seems to be provided. We welcome such a possibility and find that it should be possible to phase-in the clearing obligation for the insurance sector last due to the robustness of the sector making the risk of a late phase-in minimal.

Yours sincerely,

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