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| 11 July 2014|2014/800 Reply Form |

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| Reply form to the Consultation Paper on the Clearing Obligation under EMIR (no. 2) |
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| Date: 11 July 2014  2014/800 Reply Form |

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 (n0. 2), 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 September 2014.**

All contributions should be submitted online at [www.esma.europa.eu](http://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](http://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

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| --- | --- |
| Name of respondent | ASSOSIM – Associazione Italiana Intermediari Mobiliari |
| Are you representing an association? | Yes |
| Activity | Other Financial service providers |
| 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).

ABI and ASSOSIM agree with the bottom-up approach for the clearing obligation.

ABI and ASSOSIM are concerned about the chances that a small financial intermediary belonging to Category 2 will not be able to find a clearing member willing to offer clearing services. This case might be less probable for Interest Rate Swaps, but the industry highlights the fact that for CDS it might be a real possibility due to the lower volume traded by small intermediaries on such instrument.

Therefore, we are wondering what would happen if a small financial intermediary belonging to Category 2 will not be able to set a contractual relationship with a clearing member.

<ESMA\_COMMENT\_1>

# The clearing obligation procedure

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

<ESMA\_QUESTION\_1>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_1>

# 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.

<ESMA\_QUESTION\_2>

Yes, we agree with the proposed option. So, we welcome the solution to include the new series since the outset on a systematically basis. This would also make easier to identify the relevant contracts.

<ESMA\_QUESTION\_2>

# 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.

<ESMA\_QUESTION\_3>

Yes, we believe so.

As regards the second part of question no. 3, we do not believe that single name CDS should be a priority for the first determination.

<ESMA\_QUESTION\_3>

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

## 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?

<ESMA\_QUESTION\_4>

It is of the utmost importance that the clearing obligation enters into force only once at least two CCPs have been authorized to clear the relative derivative classes.

<ESMA\_QUESTION\_4>

## 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.

<ESMA\_QUESTION\_5>

Yes, we agree with the proposal to have one single definition.

Moreover, with the intention to stress the position already expressed in the answer to the consultation paper no. 1 on IRS, we report the following. 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 fall into a specific category (*e.g.* Category 1) for the asset classes for which it is a clearing member and into another category (*e.g.* Category 2) for the other asset classes for which it is not a clearing member.

<ESMA\_QUESTION\_5>

## 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.

<ESMA\_QUESTION\_6>

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 members have gathered more evidence to base their decisions as to whether participate 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 remarks 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 members 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 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 a 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 of the consultation paper no. 1 on IRS, for the time being, the indirect clearing activity remains undeveloped and, as stated in paragraph 214 of the consultation paper no. 1 on IRS, 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 high 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, cooperatives 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, will *de-facto* be not able to keep an efficient risk management activity 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 characterized 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). Indeed, 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 economic conditions (*i.e.* fees, margins/collateral) to access clearing (in relative terms to the volume of operations of small banks).

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 and non-clearing members 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\_6>

# 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.

<ESMA\_QUESTION\_7>

ABI and Assosim propose to not foresee any frontloading activity for intermediaries falling into Category 2.

The frontloading period should only apply to contracts entered into or novated between two Category 1 counterparties.

On the frontloading issue, please consider that even though counterparties entering into or novating OTC derivatives in Period B[[1]](#footnote-1) will know:

1. the classes of derivatives that will be subject to the clearing obligation,
2. the CCPs currently authorised or recognised to clear those derivatives,
3. the date on which that obligation begins to apply and
4. the minimum remaining maturity at that date above which the clearing obligation applies,

market participants will still be unable to accurately price trades that will be cleared at a future date.

Indeed, the pricing is complicated by the fact that a counterparty may not have a clearing arrangement in place at the time the clearing obligation takes effect. Because clearing members are likely to be unwilling to pre-commit to clear the contract when the clearing obligation becomes effective, dealers cannot be sure that the trade will be cleared at all. If the client has not been able to put the requisite clearing arrangements in place by the time the clearing obligation takes effect, the trade may end having to be torn up.

The upshot of being unable to price swaps accurately means that trades will undergo pricing adjustments when frontloaded into clearing houses, forcing market participants to make rebalancing payments. The problem is, in the event that the large part of the industry (Category 2 firms) were to backload their trades on the date that the clearing obligation takes effect, the market would be swamped – calculating, negotiating and executing balancing payments on a multilateral basis would be an unworkable enterprise for both an individual firm and the industry as a whole. Individual firms would simply not have the bandwidth to negotiate potentially hundreds of portfolios on a single day.

Concurrently, the risk that some counterparties may not have been able to put clearing arrangements in place by the time the CO takes effect, in combination with pricing and valuation uncertainty, could force very large numbers of contracts to be required to be terminated or assigned. This requirement would arise simultaneously at the CO date for all trades remaining un-cleared, causing major disruption and having a detrimental effect on the stability of financial markets.  The legal and operational process surrounding this implied mass termination exercise would be considerable, with dealers being requested to provide potentially thousands of independent valuations, and would be exacerbated by the feedback loop from pricing uncertainty which would introduce an element of contention into the calculation of close-out amounts.

<ESMA\_QUESTION\_7>

# 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.

<ESMA\_QUESTION\_8>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_8>

# Annex III - Impact assessment

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

<ESMA\_QUESTION\_9>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_9>

1. Any trade with a minimum remaining maturity (MRM) of six months or more, entered into or novated on or after the date of publication of the RTS in the Official Journal of the European Union. [↑](#footnote-ref-1)