

ING response to the draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories

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About ING

ING is a global financial institution of Dutch origin, offering banking, investments, a variety of life insurance, non-life insurance and retirement services to meet the needs of a broad customer base. Going forward, we will concentrate on our position as an international retail, direct and commercial bank, while creating an optimal base for an independent future for our insurance and investment management operations.

With more than 94,500 employees, we serve over 67 million private, corporate and institutional customers in over 40 countries in Europe, North America and Latin America, Asia and Australia.

We draw on our experience and expertise, our commitment to excellent service and our global scale to meet the needs of a broad customer base, comprising individuals, families, small businesses, large corporations, institutions and governments.

Key remarks

ING welcomes the opportunity given by the ESMA to comment on the draft technical standards for the regulation of OTC Derivatives, CCPs and Trade Repositories.

In our opinion maximum effort should be made to harmonise reporting requirements with Dodd Frank and other global requirements. Maximum harmonisation of the time frame with other jurisdictions (US in particular) is very important to avoid regulatory arbitrage and unlevel playing field. This includes data fields (LEI, UPI, etc), information sharing agreements, or single use of a GTR for DF and EMIR.

Furthermore, the timing of EMIR should also be synchronized with CRD IV implementation. This is relevant for instance for dispute resolution requirements and the availability of eligible CCPs.

With regards to Indirect Clearing Arrangements, a clearing member should be free to decide whether it wants to (i) clear only its own proprietary positions (ii) provide client clearing services only or (iii) facilitate also indirect client clearing.

Once a clearing member makes the business decision, it has to comply with the standards applicable to the services it has decided to provide.

ING proposes that the technical standards specifically clarify, under what circumstances a swap that is used to change the nature of interest on a financial liability will qualify as a hedge for the purposes of EMIR.

On CCPs, ING recommends to add the extra general requirement that a CCP should give full disclosure to the regulator and their clearing members upon request on how it calculates initial margin in terms of models and model input details upon request.

ING is supportive of the fact that the ESMA document already addresses concerns around duplication of reporting requirements with MIFID, so it is good to see that acknowledged with the proposal that TRs act to satisfy both regulatory requirements.

ING does not believe the tremendous reconciliation effort that the current draft guidelines propose is balanced appropriately with the added value of such reconciliations especially with regard to (often non-financial) counterparties with less than 300 OTC Derivatives. A more detailed substantiation and alternative proposal is included in the following pages.

With regard to TRs, ING recommends that all items in the section on exposures (section 2e) should – in line with the referenced article 11 – only apply to (collateral exchanged in the context of) OTC Derivatives.

ING detailed response

OTC DERIVATIVES

P9/III.II Clearing obligation procedure

ING supports proposition of ESMA in paragraph 20 that “clearing obligation will actually enter into force following the bottom-up approach”.

P14-15/III.V Non-financial counterparties

According to the consultation paper (III.V point 57) “...a derivative contract entered into by an NFC is deemed objectively measurable as reducing risks when the accounting treatment of the derivative contract is that of a hedging contract pursuant to IFRS principles as referred to in IAS39..”.

In order to avoid uncertainty in this area, ING proposes that these technical standards specifically either confirm, or otherwise clarify, under what circumstances a swap that is used to change the nature of interest on a financial liability (e.g. swapping a fixed rate bond into a floating rate bond) will qualify as a hedge for the purposes of EMIR.

P21/III.VI Risk mitigation for OTC derivative contracts not cleared by CCP – intragroup exemptions

ING supports wide intra-group exemption and stresses the importance that such exemption may be applied for **well before** the margining and clearing obligations are effective so that parties have sufficient time to make an application. Parties should be able to apply for intra-group exemption on a general basis and for a wide scope of transactions.

ING also likes to point out:

- possible difficulties in determining “the anticipated size, volumes and frequency of OTC derivative contracts per annum” as specified in the Article 7(2)(e)(vii) RM – given the volatility and change of the business due to the global regulatory reform.
- It is not clear how frequently “the notional aggregate amount of the OTC derivatives contracts for which the intragroup exemption applies” should be measured and published as this figure is dynamic and will constantly change.

P 48/273:

d. In practice, collateralisation at ING is mostly done on portfolio level. Proposed reporting requirements seem to imply collateral is posted at trade level. We would like to see clarification whether ESMA would like to get the total amount of collateral being replicated for each trade line, or whether they would like to receive the total amount of collateral once, for instance per counterparty legal entity.

Appendix V (P144)

27 Collateralisation

U=uncollateralised, PC= partially collateralised, OC=one way collateralised or FC- fully collateralised.

28 Collateral basis

Y=Yes / N=No.

29 Collateral type

C=cash, S=securities, B=bonds, M=mixed, O=Other.

30 Other Collateral type

Free text.

31 Collateral amount

Indicates the amount of collateral that is posted by a counterparty

32 Currency of collateral amount

E = Euros, US = US dollars, UK = Pound Stirling, O = Other

e. 'whether there is an obligation to clear" how could we indicate this on trade level? Would this mean we need to create our own clearing eligibility rules? This aspect needs to be further clarified in the ESMA standards.

f. are there clear definitions on what is considered intragroup?

In addition ING has concerns around getting the full data field population populated correctly for existing "open" contracts which need to be back reported; depending on the age of the contracts, retrieval of the data could be time consuming.

P51/296:

TRs will probably do the matching of the submitted reports. It is not yet clear from the document how this will work: how will mismatches be communicated, what obligations will a bank have towards its counterparties, dispute mechanism and so on.

P64: (portfolio compression)

20. In accordance with paragraph 86 on page 19 and article 3.2 on page 74, ING suggests to make more explicit that the requirement to perform portfolio compressions at least twice a year is subject to exceeding the 500 trades threshold.

P66: (indirect clearing arrangements (ICA))

ING supports further clarification of an indirect client relationship in the tiered participation arrangement. ING believes that ICA should provide for the detailed rules of indirect protection which would allow indirect clients to be protected both from the default of a clearing member and a client.

However, ING has serious reservations on mandating clearing members "*to facilitate indirect clearing arrangements on reasonable commercial terms*". Instead clearing members should be able to make a business decision whether to facilitate an indirect client or not. It should be noted that a clearing member clearing its proprietary positions at CCP can make a business decision whether to provide client clearing or not. This decision depends on the level of services that an institution wants to provide (e.g. clearing brokerage vs. execution brokerage only). In the same manner a clearing member providing client clearing services should be free to decide whether it wants to provide services also for indirect clients. Once the clearing member makes the decision to provide services to indirect clients then it should be in position to comply with all the requirements of ICA.

ING does not believe that mandating indirect client clearing facilitation to clearing members is necessary from a policy objectives perspective as there is enough market incentive to

provide indirect client clearing for sophisticated institutions (as ESMA claims in the paragraph 17 “arrangements allowing for the clearing of transactions of indirect clients (i.e. the clients of clients of clearing members) are not uncommon in the EU”)

In summary we believe that:

- A clearing member should be free to decide whether it wants to (i) clear only its own proprietary positions (ii) provide client clearing services only or (iii) facilitate also indirect client clearing.
- Once a clearing member makes the business decision, it has to comply with the standards applicable to the services it has decided to provide.

P73/P74: (reconciliations)

The proposed requirement is to daily reconcile all OTC Derivatives portfolios with 500 trades or more, weekly reconcile portfolios between 300 and 500 trades and monthly reconcile portfolios with less than 300 trades. We would like to point out that this tremendously increases the reconciliation burden. In current market practice, the reconciliation efforts focus on OTC Derivatives done under CSAs. The ING bank entities currently have approx. 700 to 800 CSA counterparties with which OTC Derivatives are regularly outstanding covering a total of 115,000 trades (including trades cleared via LCH). ING currently has approx. 6,000 to 7,000 non-CSA counterparties with which OTC Derivatives are regularly outstanding which are covering a total of around 60.000 trades (often only 1 trade per non-CSA counterparty). In an effort to balance the extra effort against the added value of reconciling these 'smaller' (often non-financial) counterparties, we propose the following for the category counterparties with less than 300 OTC Derivatives:

- for non-financial counterparties: Upon request of the non-financial counterparty (who often cannot value their trades independently), financial counterparties should deliver an overview of the outstanding OTC Derivatives (including mark-to-markets).
- for financial counterparties: Portfolio reconciliation should take place in the context of disputes that arise in the margin call process or at the discretion of either counterparty involved in the trades.

In general, we would like to propose that Intercompany counterparties reconciliations should be performed at the discretion of the entities involved (as these intercompany entities generally use the same systems and methods for recording and valuing the applicable trades).

P74/75: (dispute resolution)

4.2/3 ING proposes to bring this article in line with Basel 3 / CRD IV. The procedures that have to be in place between parties for disputes not solved within 5 days and the reporting obligation of disputes lasting longer than 15 days (and higher than EUR 15 mln) are not in line with the minimum holding period / margin period of risk of OTC Derivatives of 10 days under Basel.

4.2c. ING proposes to include specifically in this article that the dispute resolution wording in the CSA and/or the industry protocol on dispute resolution (like the ISDA Collateral Disputes Resolution protocol) will qualify to cover for these requirements.

CCP's

P105:

1. The 99.5 % confidence interval with regard to the initial margin calculation for OTC Derivatives is not in line with Dodd-Frank (which refers to 99%). As this would create arbitrage possibilities and difficulties when determining a portfolio margin, the respective confidence levels should be brought in line.

P106:

1a. In order to not unnecessarily drain liquidity from the market, ING suggests to change the right of a CCP to allow for offsets when margined products are correlated into an obligation.

P111:

1: We recommend that an explicit definition of minimum required credit quality is included in the assets eligible as highly liquid collateral.

1.1. We propose not to go any lower than the referenced 50%.

P112:

3.b.vii.1 Though it has been mentioned in previous consultation rounds, we recommend that 100% correlated covered bonds (issued by the party placing the collateral) not to be regarded as 'highly liquid collateral'. Additionally, we would broaden the subcategory that is not regarded as "highly liquid collateral" and defined as "financial instruments that are issued by the clearing member providing the collateral" by replacing it with "financial instruments that are issued by any clearing member of the CCP". The reason for this is that we do not deem it prudent to accelerate the risk in a CCP if one of their members is in trouble. Besides having to deal with a possible default of one of its members, the CCP may be exposed to increased counterparty risk on its other clearing members from which it has accepted collateral issued by the member in trouble, as the value of that collateral will likely decrease simultaneously.

P114:

CCPs and clearing members should accept the use of Central bank guarantees to fulfill collateral and default fund obligations. In this concept, the Central Bank issues a guarantee for the obligations of the clearing members, who on their part will issue a counter-guarantee secured by collateral deposited with the Central Bank. The use of central bank guarantees results in the advantages of efficient use of collateral as a result of pooling this with the Central Bank and mitigation of concentration risk on CCPs and clearing members.

P116:

1b. ING recommends that an explicit definition of minimum required credit quality should be included in the Investment Policy of the CCP.

TRADE REPOSITORIES

P137:

3) Our proposal is to make it explicitly mandatory that a unique trade identifier must be assigned on the day of inception of the trade.

P140:

6.1. In order to comply with the requirement of reporting all collateral exchanged, ING would advise to extend Table 2 with repetitive fields for collateral type, collateral amount and currency of collateral amount (instead of referring to 'other').

6.2 ING recommends that the key specific collateral amount that should be reported should (at least) be the market value before haircut. In addition, the nominal value and the market value after haircut could be included as separate fields to enrich the data in the trade repository.

P142:

2. ESMA should make clear whether they want to have the counterparty ID filled in separately for each branch of a Bank or to have it on Head Office or legal entity level. In case of having it on branch level (gives an indication of the regional consequences of a trades), then we assume ESMA keeps some kind of GRID system in place that links up all branches to the correct Head Office, with no other field currently requested to provide this information.

8. ING is looking for clarification on what type of notional is used for amortising contracts: it is not clear whether the original notional amounts or the current notional amounts (or maybe even the maximum notional on a forward looking basis). Some derivatives have multipliers on their pay-offs. In systems this can sometimes be represented by doubling the notional, but there is also the possibility to account for this in a “multiplier” field. ESMA needs to make explicit how to have this accounted for. Please note further that some more complex products have a call side of 100 combined with a put side of 2 x 100. The question then becomes what is the trade notional for both counterparties to the trade, given that the trade will have only 1 trade ID.

13. A slightly related issue is the “counterparty side” information. In case of packaged trades, ESMA should make explicit, whether they want to have the package send to a TR in a deconstructed way or make more specific what is expected here. For instance, in case a bank sells a call and buy a put in one package (frequently happening), then it is not clear what ESMA expects to receive in the TR (1 trade, or 2 trades, and if 1 are they interested in the long side or the short side?).

P144/145:

16. In our opinion it should be made clear whether possible break clause(s) in trade confirmations should be recorded in the Termination Date field.

27. To apply either the option FC (fully collateralized) or PC (partially collateralized), ING recommends that - especially in the context of master agreements – only thresholds above EUR 5 mln should lead to a value PC (partially collateralized). We strongly discourage that the possible existence of disputes should be taken into account in determining the value FC or PC (which would make this field subject to change on a daily basis).

31 Our proposal is to have the collateral amount to be reported to be the amount at the Close Of Business T-1. In addition ING proposes to make more explicit that amounts held and posted should be reported.

34. References to the difference between the closing price and the current market price make sense in the context of listed (exchange traded) derivatives. However, in the context of OTC

Derivatives (cleared or uncleared), referring to the mark-to-market would make more sense. Also, ING would advise ESMA to include the currency of the MtM as well as to provide clarity on the frequency of updating MtMs.

36. It is unclear what is meant by a 'different' master agreement than the 'master agreement identified in field 18'.

In general, ING recommends that the items in (section 2e- exposures, items 27 to 34) should – in line with the referenced article 11 – only apply to (collateral exchanged in the context of) OTC Derivatives.

P146:

47/48: It is unclear from the text whether the two rows stand for the near and far leg of FX swaps. Our suggestion is to make this more explicit.

P274:

On the principal side there is the point that, even with perfect trade information the TRs will not be able to generate exposure figures because they do not have the appropriate measurement systems in place to translate the trades into some meaningful exposure figure, so there is a reason for ESMA to ask banks to add this next to their trade data. However in order to make things comparable, banks have to agree on a common ground for measurement. Even if ESMA allows different banks to use their own proprietary exposure measurement, there are still questions open as to what measure should be provided (positive expected exposure, negative expected exposure, or quantile exposures just to name a few alternatives). Therefore ING thinks this information should not be asked for from day one. Our advice to ESMA is to first work with existing trade information in order to gain experience on whether existing information is sufficient.