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Consultation Paper: Review of technical standards on reporting under Article 9 of EMIR

Dear Sirs,

We welcome the publication of ESMA's Consultation Paper *Review of technical standards on reporting under Article 9 of EMIR* (the "***Consultation Paper***" or the "***CP***") and we appreciate the opportunity to provide you with our comments.[1]

Markit is a leading global diversified provider of financial information services. We provide products that enhance transparency, reduce risk and improve operational efficiency. By setting common standards and providing shared solutions that facilitate market participants' compliance with regulatory requirements, many of Markit's services help level the playing field between small and large firms and herewith foster a competitive marketplace.[2] Our customers include banks, hedge funds, asset managers, central banks, regulators, auditors, fund administrators and insurance companies. Founded in 2003, we employ over 3,500 people in 10 countries. Markit shares are listed on Nasdaq under the symbol MRKT.

Markit has been actively and constructively engaged in the debate about regulatory reform in financial markets, including topics such as the implementation of the G20 commitments for OTC derivatives and the design of a regulatory regime for benchmarks. Over the past years, we have submitted more than 115 comment letters to regulatory authorities around the world and have participated in numerous roundtables. We also regularly provide relevant authorities with our insights on current market practice, for example, in relation to valuation methodologies, the provision of scenario analysis, or the use of reliable and secure means to provide daily mid-market marks. We have also advised regulatory authorities on appropriate approaches to enabling a timely and cost-effective implementation of newly established regulatory requirements, for example through the use of multi-layered phase-in or by providing market participants with a choice of means for satisfying regulatory requirements.

Introduction

Our below comments on several issues raised by ESMA in the Consultation Paper are based on the experience we have gathered by providing the following services:

- Markit's derivatives processing platforms facilitate confirmation, matching and processing for OTC derivatives across regions and asset classes and provide universal middleware connectivity for

[1] ESMA Consultation Paper: Review of technical standards on reporting under Article 9 EMIR. ESMA 2014/1352. 10 November 2014.
[2] For example, Markit's KYC Services provide a standardized end-to-end managed service that centralizes "Know Your Client" (KYC) data and process management.

downstream processing such as clearing and reporting. Specifically, the MarkitSERV[3] platforms (1) facilitate the agreement[4] between parties on the details of the transactions that they have entered into, (2) provide them with connectivity to CCPs,[5] trading venues and inter-dealer brokers, trade repositories ("***TRs***"), and the whole range of counterparties, including buyside and sellside, and (3) report the relevant transaction and counterparty details to trade repositories under newly established regulatory requirements.[6] Such services that are also offered by various other providers are widely used by participants in the global OTC derivatives markets today and are recognized as tools to increase efficiency, secure legal certainty, and reduce cost. With globally over 1,500 firms using the various MarkitSERV platforms that process, on average, 80,000 OTC derivative transaction processing events per day, our legal, operational, and technological infrastructure plays an important role in supporting the OTC derivatives markets in Europe, North America, and the Asia-Pacific region.

- For many years, participants in the credit default swaps ("***CDS***") markets have used Markit's CDS reference data products[7] such as Markit RED codes to accurately manage CDS transactions through the product lifecycle, managing both entity and obligation data. Based upon feedback from our client base of over 400 institutions we are currently working with several regulatory bodies on a global requirement of a UPI for credit markets. This may be involving but is not limited to unitizing aspects of the current CDS RED service. Further, market participants use our CDS sector data to aggregate sector performance and risk. ESMA should note that we have discussed the use of our CDS sector data alongside the ISDA Taxonomy with industry associations to assist with transaction reporting across multiple jurisdictions. We have also begun to integrate LEI data into our product offering to assist participants and regulatory bodies with data aggregation. As provider of reference data and as administrator of Standard Reference Obligations ("***SROs***")[8] for the CDS markets we aim to ensure that such markets operate in a clearly defined and safe manner. We stand ready to support the industry in the multiple challenges faced by upcoming regulatory requirements. We encourage ESMA to carefully consider evolving industry standards and reflect them in the fine-tuning of the reporting requirements under EMIR but also its approach to making use of the data.

Comments

We welcome ESMA's initiative to review the application of some of the Technical Standards related to the reporting of derivative transactions under Article 9 of EMIR. We agree with ESMA that the current regime might contain some shortcomings and there might be "particular instances where improvements could usefully be made".[9]

[3] MarkitSERV, a wholly owned subsidiary of Markit Group Limited, provides a single gateway for OTC derivatives trade processing. The company offers trade processing, confirmation, matching, and reconciliation services across regions and asset classes, including interest rate, credit, equity, and foreign exchange derivatives. MarkitSERV also connects dealers and buy-side institutions to trade execution venues, CCPs, and trade repositories. Please see www.markitserv.com for additional information.

[4] Depending on the asset class and type of execution, different methods will be used to achieve such "agreement", including affirmation/confirmation or matching.

[5] Our processing platforms are currently connected, or are planning to connect, to more than 10 CCPs around the globe and in various asset classes.

[6] Our processing platforms currently report derivatives transactions for the reporting parties to Trade Repositories in Europe, the United States, Japan, Hong Kong, Australia, and Singapore.

[7] Markit Reference Data confirms the relationship between a reference entity and a reference obligations, as well as corporate actions, CDS succession events and credit events. We also provide verified index and constituent information for credit indices, including updated weighting and index factors upon a credit event. More information *available at* http://www.markit.com/Product/Reference-Data-CDS.

[8] Markit is the appointed SRO administrator working in partnership with ISDA to assist the determinations committees in each region to support its role in SRO rules. In accordance with the SRO rules Markit provides a service to publish the SRO list and support the relevant determinations committee in (although not limited to) the following: processing SRO requests, SRO endorsements, SRO substitutions, SRO challenges and SRO rejections. More information *available at* http://events.markit.com/std-reference-obligation-registration.

[9] CP, p.4

In addition, given its role in the upcoming EMIR Review,[10] we expect ESMA will start considering the need and potential for making also some more fundamental changes to the EMIR reporting obligations. We suggest that such changes could include a potential switch to a single-sided reporting approach and adjustments to the reporting of CDS to reflect the increased use of SROs:

- **Double- vs single-sided reporting**

Based on our experience in reporting OTC derivatives transactions to Trade Repositories in a variety of jurisdictions around the globe, we recommend considering switching from the current double-sided to a single sided-reporting regime in Europe. This is because the double-sided reporting obligation under EMIR has proved to not only impose a very significant burden on smaller market participants but also reduce the quality of the data that is captured in TRs.

Such change could most easily be achieved by providing exemptions to certain categories of market participants for transactions that their counterparties already report. This would be consistent with what is being considered in some other jurisdictions that had also initially chosen a double-sided reporting regime.[11] We would expect a switch to an effectively single-sided reporting obligation to resolve several issues that we have observed in the context of TR reporting under EMIR,[12] improve the quality of the reported data and reduce the burden on market participants. Additionally, such change could lead to increased international consistency of reporting regimes.[13]

- **The increasing relevance of SROs**

Today, on any report of a CDS transaction to a European Trade Repository, we will report both the ISIN and the reference entity name for the underlying field. Only the ISIN will be sent to the relevant regulatory authority though, as this is the only information that the regulator has previously requested and TRs are able to send.

ESMA should note that an industry move is underway towards establishing Standard Reference Obligations ("***SROs***") for reference entities in the CDS market. The use of SROs will benefit the marketplace from a risk and efficiency perspective by reducing the number of confirmation breaks and improving the timeliness of the matching of transaction details. Currently, the ISDA DC is in the process of reviewing and agreeing SROs per entity/tier combination to be referenced on all current, active and future trades. If any future changes or

[10] "According to Article 85(1) of EMIR, the Commission should review and prepare a report by 17 August 2015 on EMIR and should co-ordinate with ESMA on a number of aspects. It is therefore expected that the EC will request ESMA to provide technical advice on the EMIR review." See ESMA 2015 Work Programme, http://www.esma.europa.eu/system/files/2014-1200_-_esma_2015_work_programme.pdf

[11] For example, ASIC in Australia now actively considers exempting smaller firms ("phase 3c") from the reporting obligation in case their counterparty has reported the transaction, which would transform their regimes effectively almost into single-sided regimes. Other jurisdictions might also outline detailed plans in relation to reporting obligations for the smallest firms.

[12] Based on our experience in reporting derivatives transactions to TRs for a large number of market participants and in various jurisdictions, we have noticed the following issues in relation to double-sided reporting under EMIR: (1) level of preparedness: small firms in Europe that enter into OTC derivatives transactions are often ill-prepared to report and, sometimes, still not even aware of their obligations. This will often result in misreporting, mismatches and duplication; (2) relevance of delegation: market participants appreciate the fact that EMIR explicitly allows for the delegation of reporting to the counterparty or a third party ("In order to allow flexibility, a counterparty should be able to delegate the reporting of the contract to the other counterparty or to a third party." Draft regulatory technical standards on trade repositories.) However, many dealer counterparties are averse to performing such reporting for a client by agreement with the client maintaining the obligation; and (3) UTI exchange: the UTI exchange generally works well for electronically traded and electronically confirmed transactions, e.g., confirmed via middleware such as MarkitSERV. However, it has proved to be challenging for transactions that are confirmed on paper which is the most common approach used by smaller firms. Issues also exist in relation to specific types of flows, e.g., for a principal-model client-cleared transaction between the Clearing Broker and the client. Failure of UTI exchange will cause duplicative reporting for these situations.

[13] We recommend close coordination with other international regulators in this context, in particular with the CFTC, given that it is currently also in the process of fine-tuning its reporting regime.

updates are made to the SRO, confirmed trades that already use a SRO would be automatically updated to reference the most recent version. ESMA should further note that, once SROs have been established, the ISIN will become somewhat meaningless for these names. Also, multiple trades on different reference entities might be reported with the same dummy identifiers[14] and some reference entities might trade with no reference obligation at all. In these situations the reporting of ISINs will not enable the user to understand the exposure that has been traded. Markit is committed to working with the industry to provide an efficient and effective solution in this respect and help facilitate the reporting of the underlying ISIN and/or reference entity LEI information to the relevant regulators.

That said, please find below our comments related to specific clarifications and adaptations of the existing EMIR reporting requirements.

Adaptations

Question 4: Do you think the adaptations illustrated in this section adequately reflect the derivatives market and will help improve the data quality of reports? Will the proposed changes cause significant new difficulties? Please elaborate.

- **Notional amount**

ESMA proposed amending and renaming the current Table 2 Field 14, “Notional amount”, and introduce a new field for notional.[15] Specifically, ESMA proposed using the following two fields[16] in relation to the reporting of the notional amount of the transaction: (1) the “original notional” would reflect the reference amount from which the contractual payments were originally determined whilst (2) the “actual notional” would represent the current reference amount from which the contractual payments would be determined in case that the terms of the initial contracts have changed.

We believe that market participants would benefit from additional clarification regarding this adaptation. For example, it is not clear whether ESMA expects counterparties to report a factored down notional for a CDS in case of a credit event. In this context, ESMA should be aware that this is not market practice today in any other reporting regime or for confirmation purposes.

- **Action type**

ESMA stated that “when termination takes place at the original date, there is no need for a report stating the termination of the contract at the original date, which leads to confusion regarding the description of the Action type - Cancel.” It therefore proposed “that the description and content of that field should be adapted to clarify the use of the different values.”[17]

We encourage ESMA to provide further clarification on this issue. If ESMA wanted to clarify that, once a derivative contract reaches its *scheduled termination date* and ‘dies naturally’, there is no need to report such event as a termination, we agree with its clarification. However, as written it might seem that, in cases where counterparties enter into transaction and decide later *that same day* to terminate it, this termination would not need to be reported. In our experience, this is not an uncommon occurrence in the CDS markets and we believe such type of termination should be reported.

[14] For example, XSSNRREFOBLO and XSSUBREFOBL0.
[15] CP, par. 34.
[16] Table 2, Fields 19 and 20
[17] CP, par. 39.

ESMA also seems to suggest that "an early termination of an existing contract" should be identified as "cancel".[18] However, we believe that such event should be identified as "termination" and not as "cancel". This is because "termination" is an established term used amongst industry participants and it is also used in other reporting regimes.

Introductions

Question 5: Do you think the introduction of new values and fields adequately reflect the derivatives market and will help improve the data quality of reports? Will the proposed changes cause significant new difficulties? Please elaborate.

Q8: Do you envisage any difficulties with the approach described in paragraph 45 for the identification of indices and baskets? Please elaborate and specify what would be the most practical and industry consistent way to identify indices and baskets.

- **Underlying field**

For transactions in CDS indices or baskets, ESMA seems to suggest that reporting parties report the ISINs for the bonds underlying *all* index or basket constituents.[19] We believe that such requirement would create an unnecessary burden for the reporting parties whilst not adding any value from a regulatory perspective. We therefore recommend that, to uniquely identify the CDS index that was traded, reporting parties report "the full name of the index as assigned by the index provider, or ISO 6116 ISIN, where available".

Q9: Do you think the introduction of the dedicated section on Credit Derivatives will allow to adequately reflect details of the relevant contracts? Please elaborate.

Given the specificities of the different categories of derivatives we generally welcome the introduction of a dedicated section on credit derivatives. That said, our comments and suggestions in relation to specific elements of Section 2i of Table 3 are as follows:[20]

- **Coupon**

    - ESMA proposed requiring the reporting of "the fixed coupon of the contract in percentage".[21] ESMA should note that not all transactions in CDS will have a coupon associated with them.[22] We therefore encourage ESMA to clarify how this field should be populated in such cases. Specifically, we suggest that "zero" could be used in this field in case that no coupon has been fixed for the CDS transaction.

- **Date of last lifecycle event**

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[18] "An early termination of an existing contract, in which case it will be identified as 'cancel'". Line 73, Table 2, Common Data.

[19] CP Par. 49. "Equally, the identification of Baskets or Indices should be more granular to allow national competent authorities to perform a more accurate assessment of data. Indices must always be identified with ISINs where available; otherwise, the full name of the index as assigned by the index provider should be indicated. For baskets composed, among others, of financial instruments traded on a trading venue, it is proposed to identify each such individual financial instrument with a view to align this reporting requirement with the upcoming MiFIR transaction reporting requirements."

[20] CP, Table 2: Common data.

[21] Line 69, Table 2, Common Data.

[22] This might be the case, for example, for "recovery locks" or some tranches of structured CDOs.

- We encourage ESMA to provide further clarification on what exactly this field shall cover. For example, it is not clear whether it should just be used for credit events, re-names and re-organisations (which would be described as “lifecycle events” in industry parlance) or whether ESMA’s intention was for this field to capture a broader range of events, e.g., to also be used for events such as terminations and assignments.

- **Index factor**

  - ESMA required “the factor to apply to the Actual Notional (Field 14b) to adjust it to all the previous credit events in that Index series.”[23] We believe that, if regulators were provided with an index factor that reflects previous credit events, there would be no need for the reporting of the actual notional of the transaction. We therefore encourage ESMA to clarify why the reporting of both fields is necessary and, unless there is a valid reason for the reporting of both, only require the reporting of one of them.

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We hope that our above comments are helpful to ESMA. We would be more than happy to elaborate or further discuss any of the points addressed above in more detail. In the event you may have any questions, please do not hesitate to contact us.

Yours sincerely,

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[23] Line 73, Table 2, Common Data.