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European Securities and Markets Authority
103 Rue de Grenelle
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19 March 2012

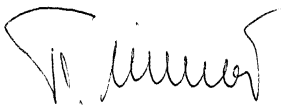
Re: Discussion Paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories

Dear Sir/Madam,

UBS would like to thank ESMA for the opportunity to comment on the Discussion Paper on Draft Technical Standards for the Regulation of OTC Derivatives, CCPs and Trade Repositories. Please find attached our response to the questionnaire.

We would be happy to discuss with you, in further detail, any comments you may have. Please do not hesitate to contact Gabriele Holstein on +41 44 234 4486.

Yours sincerely,
UBS AG



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UBS Response to ESMA's Discussion Paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories

INTRODUCTION

UBS would like to thank ESMA for the opportunity to comment on the discussion paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories. Please find below our response to the overall content, as well as the specific questions set out in the Paper.

UBS General Views on Clearing and CCP requirements

On a more general note we would like emphasize our view that the ultimate goal of Clearing should be to support financial stability in a fair and efficient market infrastructure embedded within a regulatory framework. There are a number of prerequisites to reach this goal which we have outlined below.

Prerequisites for financial stability

In our view financial stability can only be achieved where

(i) Membership requirements are strictly defined. Clearing members underwrite the integrity of the CCP structure and their ability to support a strong risk management framework needs to be ensured;

(ii) The CCP default process to be followed in the event of client and clearing member default is clearly defined and as such transparent and predictable;

(iii) Initial Margins are set at an appropriate level. It is important to ensure that CCP's are not allowed to compete on margin levels;

(iv) The CCP's risk management framework incorporates feedback from the CCP risk committee;

(v) CCP Capital is set at an appropriate high level. CCPs are systemically important institutions and as such it needs to be ensured that they are appropriately capitalized and incentivized to risk manage effectively by being impacted high in the waterfall ahead of the Default Fund contributions;

(vi) Client Segregation Options do not force Clearing members towards a path of Super Segregation. We believe that such a requirement is likely to have unintended consequences with Banks withdrawing from offering clearing

services. We advocate a segregation framework that gives our clients sufficient protection for portability whilst making it an economically viable solution.

Prerequisites for a fair market infrastructure

In our view a fair market infrastructure can only be achieved where

(i) there is a mechanism in place to differentiate between credit quality of users and clearing members in either margin levels or within the Default Fund;

(ii) a strong and and independent CCP governance is in place to deal with conflict of interest issues which arise within a commercial entity; and

(iii) there is transparency on the clearing fees charged by CCP. In particular it is important to have clarity on the split of fees where exchanges have a bundled Execution and Clearing charge. Ideally the two functions should be unbundled as different market participants use many different ways to make their all-in prices.

Prerequisites for an efficient market infrastructure

In our view a fair market infrastructure can only be achieved where

(i) Liquidity, transparency and access is maximized;

(ii) Technology solutions are scalable thereby focusing on key market structure challenges such as availability and complexity of credit limit checking and brokerage; and

(iii) there is a sensible market structure in place for the benefit of users and members not for the profitability of the CCP.

Overall, we reiterate our view that ESMA should seek consistency with US rules when establishing any process and timeline and should push for alignment across all G20 jurisdictions and beyond.

UBS's detailed responses to the specific questions posed in the paper follow below.

III. I. OTC DERIVATIVES

CLEARING OBLIGATION (ARTICLE 3)

Pursuant to EMIR, counterparties to OTC derivatives that have been concluded between third country entities that would be subject to the clearing obligation if they were established in the EU, shall clear those OTC derivative contracts that have a *direct, substantial and foreseeable effect within the EU*, or where such obligation is necessary or appropriate to prevent the evasion of any provision of EMIR.

Contracts having a direct, substantial and foreseeable 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?

It is very important that ESMA provides clarity on the scope of the extraterritorial effect of EMIR. We recognize that it is particularly important for third countries which have just initiated or are yet to initiate work on the regulation of OTC derivatives. In our view, only contracts which (i) are clearing eligible under EMIR, (ii) have an EU underlying, (iii) are above a certain trade size and (iv) have a sufficiently high level of trading activity should be considered to have a direct, substantial and foreseeable effect within the EU.

In regards to (i) we refer to our comments in Q6 and would emphasize the importance of setting the initial liquidity threshold for determining the eligibility of an OTC derivative contract for mandatory clearing as high as possible as this would minimize the probability that certain eligible contracts would no longer meet the eligibility criteria due to a reduction in liquidity or volume. If contracts repeatedly moved between being eligible and ineligible in the event of changing market information, this would be destabilising for the market. When determining the eligibility of contracts, we would also emphasize the importance that ESMA considers the economic feasibility for a clearing house and clearing brokers to offer clearing in the respective contracts. We would view the actual availability of clearing a certain product as a precondition for the clearing obligation.

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?

The most effective way to avoid evasion of EMIR is to ensure global consistency. Until the point of time that third countries have introduced EMIR equivalent provisions and have been recognized to be equivalent, we would advocate a list of "safe harbour" behaviours that are not caught by EMIR, so that participants have certainty. As an illustration, simply using (or facing) a non-EU subsidiary of an EU company should not on its own be sufficient to amount to "evasion".

Types of indirect clearing arrangements

To comply with the clearing obligation, a counterparty shall become a (i) clearing member, (ii) a client or (iii) establish indirect clearing arrangements with a clearing member. These arrangements shall not increase counterparty risk and shall ensure that the assets and positions of the counterparty benefit from the protection granted by segregation, portability and default procedure. ESMA is required to specify the types of indirect contractual arrangements that meet these conditions.

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

We strongly support the principle that indirect contractual arrangements ensure that assets and positions of the counterparty (end client) benefit from segregation, portability and default procedure.

In our view indirect contractual arrangements should have the following three key characteristics: (i) Client protection: the protection should be the same as for direct client clearing, (ii) Structure: the structure should not result in prohibitive capital or balance sheet costs for the Clearing Broker or the intermediate entity, (iii) Separation: there should not be any relationship (KYC/ AML) between the Clearing broker and the indirect client.

In regards to client protection, we would emphasize that indirect clearing set-ups are subject to similar challenges as with direct client clearing. We would draw ESMA's attention to the fact that today none of the European insolvency laws foresee special treatment of client collateral in relation to central clearing in the case of a clearing broker default. Where client collateral, both cash as well as non-cash, is passed through to the clearing house, it is exposed to the regular insolvency process and bankruptcy estate vis-à-vis the clearing broker. The one exception where client collateral enjoys special treatment on clearing broker level are the FSA Client Money and Client Asset Segregation Rules in the UK, which allow omnibus level segregation of designated client collateral. However, these rules are not appropriate for strong collateral segregation for OTC clearing by clients. The recent broker insolvencies, in particular Lehman Brothers, have highlighted the weakness of such collateral segregation rules. By contrast, in the US, clients enjoy a much more robust segregation rule in the cleared futures business. The US have, in light of the mandatory requirement for OTC clearing, further improved their rules and recently introduced LSOC (Legally Segregated Operationally Commingled) rules that give effective protection of client collateral on the clearing broker level.

The challenge is hence to establish an EU framework that allows OTC clearing with effective and efficient collateral segregation rules on the level of the clearing broker. Specifically in regards to indirect clearing, collateral treatment rules need to be adjusted to the effective nature of the role of the clearing broker and indirectly participating bank, which is the role of an agent (the clearing broker clears at the CCP, and the indirectly participating bank at the clearing broker, in its own name, but at the risk of the client). Related collateral should be treated as such in case of a default of any of these intermediaries. An additional challenge specific to indirect clearing is that the clearing member and the indirectly participating bank may operate under different insolvency laws. As such the feasibility of collateral protection solutions would need to be verified across two regulations. Also collateral protection rules for indirect clearing would need to take into consideration not only a clearing broker default, but potentially also a default of the indirectly participating bank/broker.

A solution that offers robust segregation and fast return of client assets in a clearing broker default under an indirect clearing set-up is a *deed of assignment* with all involved parties, four parties in case of indirect clearing: the CCP, the clearing member (level 1), the indirectly participating bank (level 2), and the end client. Such an agreement would, however, need to effectively rule that collateral would not flow back into the defaulted clearing broker and/or indirectly participating bank. Such a deed of assignment per end client and clearing house may, however, be problematic in its execution vis-à-vis certain insolvency laws. An alternative option could be for the client's broker/bank (indirect participant, level 2) to *pass through client collateral "on a fiduciary basis"* so that it is treated off balance sheet of the level 2 participant. Such a set-up may, however, still require a deed of assignment across all parties in order for the client to access his/her collateral effectively. A non-feasible option is, in our view, a mechanism similar to the futures & options clearing mechanisms in continental Europe where non-cash collateral is not passed through by the indirectly participating bank to the clearing member as it is associated with substantially collateral funding cost.

CLEARING OBLIGATION PROCEDURE (ARTICLE 4)

ESMA will analyse classes of OTC derivatives in order to assess the application of the clearing obligation. In order for ESMA to identify the relevant class of OTC derivatives, EMIR provides for a *bottom up approach* and *top down approach*. The discussion paper focuses on the bottom-up approach where a competent authority authorises a CCP to clear a class of OTC derivatives, and notifies ESMA. For the determination of the classes of derivatives, ESMA will, in a first stage, use as a basis the classes of derivatives defined by the CCP and the competent authorities. In a second stage, ESMA may adopt a more granular approach within these classes of derivatives. The paper sets out the information that the CCP is required to provide to the competent authority, which will in turn provide it to ESMA for the purpose of assessing:

(i) whether a class of OTC derivatives should be subject to the clearing obligation (information to include a clear identification of OTC derivative contracts and relevant class, evidence of degree of standardisation of the

relevant class of OTC derivatives' contractual terms and operational processes, volume and liquidity of class of OTC derivatives, evidence of availability of fair, reliable, and generally accepted pricing information in relevant class of OTC derivatives);

(ii) the date or dates from which the clearing obligation takes effect (information to include data on expected volume of relevant class following application of the clearing obligation; information whether other CCPs already clear the same class of OTC derivatives; evidence of ability of CCP to handle expected volume and manage risk arising from clearing of the relevant class; type and number of counterparties active/expected to be active within market for relevant class; outline of different tasks to be completed to start clearing with CCP and time expected to fulfil each task; information on risk management, legal and operational capacity of the range of counterparties active in the market).

After ESMA issues a negative assessment on the eligibility for clearing of a given class of OTC derivatives, the competent authority may submit a new updated notification if it is informed of any change in market conditions and information provided. ESMA will perform a new assessment thereafter.

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?

We believe that the information to be provided should in addition to the scope of the product also define the nature of the underlying. Specifically there should be a reference to the population of the underlying so that liquidity can properly be considered.

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?

In our view ESMA should include worst case scenarios on the basis of historic data (greatest stress points in last 10 years) as well as on the basis of a forecasted view.

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

We support the review process following a negative assessment and the opportunity to provide an updated notification, but would stress the importance of granting sufficient transition time to market participants between when a positive assessment has been made and the clearing obligation takes effect. We reiterate our view that ESMA should seek consistency with US rules when establishing any process and timeline and should push for alignment across all G20 jurisdictions and beyond.

We would furthermore welcome clarity in the reverse situation where an eligible contract would no longer meet the eligibility criteria due to a reduction in liquidity or volume. We would hence query if in such a situation there would be a status change in that the contract would no longer be considered eligible and be "delisted" and if so, immediately upon publication of the negative assessment or with a time lag. We would stress the importance to have a clearly defined time period to allow the updating of systems.

Overall we believe that it would be destabilising if contracts repeatedly moved between being eligible and ineligible in the event of changing market information. We therefore believe that it would be best to define *initial liquidity thresholds ("listing thresholds") for determining the eligibility of an OTC derivative contract for mandatory clearing at a high level* but to *determine incremental thresholds at a lower level* to flag products which no longer meet the eligibility criteria and to which higher margins would apply while they continue to be eligible "reduced liquidity flag thresholds".

Furthermore we note that ESMA has not commented on the "front-loading process". We would stress our view that we remain concerned about that practical problems of such a process. Our concern relates to the legal situation pertaining to contracts that are entered into after the date of application of the regulation, but which at the date they are entered into, have not been deemed eligible by ESMA. These contracts will be agreed bilaterally and their pricing will be contingent upon market conditions at the time. Recognition of the possibility of a future clearing requirement could only be reflected to a limited degree in relevant documentation as pricing is dependent to a significant degree on factors unique to the relevant CCP, but not known at the time of entering into the contract. Such a retroactive clearing requirement is further open to legal challenge. We would welcome clarification from ESMA as to the pricing and documentation of such trades.

Criteria to be assessed by ESMA under the clearing obligation procedure

In assessing these criteria, ESMA proposes to consider:

a. That the contractual terms standardisation refers to the use of common legal documentation, including master netting agreements, definitions and confirmations which set forth contract specifications commonly used by counterparties and operational processes standardisation refers to the extent to which product trade processing and lifecycle events are managed in a common manner to a widely agreed-upon timetable;

b. Whether the margins would be proportionate to the risk that the clearing obligation intends to mitigate and the historical stability of the liquidity through time, the likelihood that liquidity would remain sufficient in case of default of a clearing member;

c. Whether the relevant information to correctly price the contracts within the relevant class of derivatives is easily accessible to counterparties on a reasonable commercial basis including once the obligation to clear is in force.

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

On standardization, there should be commonality of standard risk factors in the contracts, and standard contract terms defined by an industry wide body.

Volume/liquidity should be assessed on the basis of combining existing open interest, average trading volume, depth of market (active market makers) as well as alternative clearing venues.

Pricing for OTC products should be assessed based on the ability to get firm levels on a daily basis from a sufficient number of clearing members

One indicator to consider in these decisions would be whether a specific contract or class of derivatives is tradeable electronically, with a significant depth of market and tradeable prices. This would indicate a good level of standardisation and liquidity for a particular contract. As a more general comment, we would also stress our view that liquidity thresholds for determining the eligibility of an OTC contract for mandatory clearing should be set sufficiently high to avoid contracts potentially moving between meeting and not meeting the eligibility criteria which could potentially destabilize markets. We refer to our comments in Q6. Furthermore there should be transparency on the number of dealers trading on a particular underlying. This is because where one or a limited number of dealers dominate liquidity; this can be seen as an indication that the product is not very liquid. ESMA should also check the methodology and quality of the pricing mechanisms.

Given the challenges of defining strict criteria on standardisation, volume, liquidity and pricing, we have listed below some examples comparing and contrasting contracts which we believe would or would not be suitable for clearing.

Example 1: a standard EUR interest rate swap to a standard tenor (3 yr, 5 yr etc) would be suitable for mandatory clearing as it has very standard terms and good liquidity. Pricing would be available from a large number of dealers, and those prices would be within a tight range.

Example 2: a standard EUR interest rate swap to a non-standard tenor (e.g. 3 yrs and 7 days) would also be suitable for mandatory clearing. This specific tenor would not appear to have good depth of liquidity because the standard "on the run" swap would be the 3 year. However, the pricing models which enable dealers to price such trades are very standardised, many dealers would be able to price it on request, and again those prices would be within a tight range. For "on the run" structures, the prices are very observable. However, before subjecting a particular OTC contract to mandatory clearing, it is essential to ensure that "off the run" structures would have a similar depth of liquidity available to them.

Example 3: a LIBOR in-arrears swap would not be suitable for mandatory clearing. Superficially, it is very similar to a standard swap. However there is not significant liquidity in these contracts and they have a level of volatility, which would be difficult for CCPs to margin appropriately.

Example 4: a 2 year into 1 year out of the money IR Swaption would not be suitable for mandatory clearing. The contract terms are very standardised. However,

- it would be important to demonstrate that each possible permutation of the contract proposed for mandatory clearing would have enough liquidity / depth of market. This swaption would not have sufficient liquidity to be appropriate for mandatory clearing.

- the pricing models for these products are much less standardised; in addition to the basic swap curve they depend on 3 further modelling dimensions. There is likely to be a considerably wider range of price levels for such contracts, depending more on each dealers proprietary view rather than observable market factors. Options which are further out of the money are likely to have increasingly wide-ranging price contributions. Long-dated options can move in/out of the money through their contract term and could therefore move from being fairly liquid to being significant illiquid and difficult to price

Public Register Available on the ESMA website

ESMA will make available on its website a public register to identify the classes of OTC derivatives subject to the clearing obligation.

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

We agree with the elements (a) to (i) to be included in the public register for the identification of clearing eligible contracts. In addition we believe that the register should include "initial listing" as well as "reduced liquidity flag" thresholds as outlined in our response to Q6.

We agree with the points to be included for the identification of CCPs and have no additions to propose.

Another point for ESMA to consider is the frequency at which the register will be updated. We believe that in addition to periodic updates, there should also be the possibility to take in / take out liquidity criteria without a full review.

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 refer to our comments in Q8.

NON-FINANCIAL COUNTERPARTIES (ARTICLE 5/7)

EMIR recognises that non-financials use OTC derivative to protect themselves against commercial risks directly linked to their commercial activities. As a result, these OTC derivative contracts that protect the non-financial against risks directly related to their commercial activities and treasury financing activities as well as those that do not protect against such risk but do not exceed a clearing threshold are not

subject to the clearing obligation. In order to calculate whether it exceeds the clearing threshold, a non-financial counterparty shall not include in its calculation the OTC derivative contracts which are objectively measurable as reducing risks directly related to its commercial activity or treasury financing activity or that of its group.

Criteria for establishing which derivative contracts are objectively measurable as reducing risk directly related to the commercial activity or treasury activity

ESMA proposes the following criteria by reference to European accounting rules. The objective of entering such derivative contracts should be to reduce the risks of:

- the potential change in the value of assets, service, inputs, products, commodities, liabilities that the non-financial counterparty or its group owns, produces, manufactures, processes, provides, purchases, merchandises leases, sells or incurs or reasonably anticipates doing the above

- the potential change in the value of assets, service, inputs, products, commodities, liabilities referred to in letter a, resulting from fluctuation of interest rates, inflation rates or foreign exchange rates.

An OTC derivative by a non-financial would also be deemed to reduce risk directly related to the commercial or treasury activity when, the accounting treatment of the derivative contract is that of a hedging contract pursuant to IFRS principles as referred to in IAS 39 paragraph 71-102 on hedge accounting as endorsed by the European Commission. Any OTC derivative in the nature of speculation, investing or trading cannot be excluded for the calculation of the clearing threshold by non-financials.

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?

Yes, we believe that ESMA's definition of legitimate hedging activities is appropriate. We would, however, query, if liability driven investment by pension funds would be classed as "reducing risk directly related to commercial activity". We would also welcome clarification if this

Clearing threshold

For the purpose of setting the clearing threshold, ESMA considers referring to the notional value of OTC derivatives subject to the clearing obligation. The clearing threshold could be set across asset classes or per asset class. ESMA therefore suggests using a threshold across all asset classes. ESMA also debates whether the threshold should be set at the level of legal entity as well as at a group level but offers no concrete proposal.

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?

No, we do not agree. We refer to our comments in Q1 and Q6 and would emphasize the importance of setting the initial clearing threshold as high as possible as this would minimize the probability that certain eligible contracts would no longer meet the eligibility criteria due to a reduction in liquidity or volume and would potentially have to "delisted". If contracts repeatedly moved between being eligible and ineligible in the event of changing market information, this would be destabilising for the market.

More specifically we believe that it would be best to differentiate between two different clearing thresholds: I*nitial listing thresholds* to be set at a high level as well as *incremental thresholds* to be set at a lower level to flag products which no longer meet the eligibility criteria and to which higher margins would apply while they continue to be eligible "reduced liquidity flag thresholds".

RISK MITIGATION FOR NON-CCP CLEARED CONTRACTS (ARTICLE 6/8)

Financial and non-financial counterparties that enter into an OTC derivative which is not subject to the clearing obligation shall mitigate risks by using different techniques. The risk mitigation techniques shall be further specified through technical standards to be developed for one part by ESMA and for another part jointly by ESMA, EBA and EIOPA. This discussion paper focuses on the risk mitigation to be specified through ESMA technical standards.

Timely confirmation

Financial counterparties and non-financial counterparties exceeding the clearing threshold should confirm, where available via electronic means, the terms of any OTC derivative entered into which is not cleared by a CCP:

a. within 15 minutes from the execution of the derivative contract, when the transaction is electronically executed;

b. within 30 minutes from the execution of the derivative contract when the transaction is not electronically executed but is electronically processed;

c. on the same calendar day for transactions that are not executed or processed electronically.

ESMA also considers that parties to transactions executed with counterparties other than those indicated above should confirm, where available via electronic means, the terms of any OTC derivative they have entered into and which is not cleared by a CCP:

a. no later than the business day following the execution of the OTC derivative when the transaction is electronically executed or processed;

b. no later than the [x] business days following the execution of the OTC derivative when the transaction is not executed or processed electronically.

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?

Yes, a transaction that is electronically confirmed is certainly faster than one that is not. Electronic trades are typically standardized and therefore so are the documentation. Non-electronically confirmed trades are typically bespoke and therefore there is bespoke language in the documentation. We note and welcome that the proposed confirmation timings are similar to those proposed by the U.S. CFTC.

We would, however, bring to ESMA's attention that certain situations may lead to a delay of confirmation cycle times or may prevent that the transaction is confirmed on a platform at all. The first is where investment managers are required to follow compliance processes and / or receive instructions from their clients, who may be subject to different timing constraints, which could take much longer than the proposed 15 or 30 minutes and in some cases may even take longer than a day. Another situation would be where a trade which could be confirmed on an electronic platform is processed on paper, because it is traded with a client which has not subscribed to the given platform. It could also be the case that certain information required in a confirmation are not known at the time of execution or for some time following the trade, e.g. fixing rates.

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

In our view more clarity is required around the definition of "unconfirmed". We would query if this refers to unexecuted trades that are not signed or matched by both sides. Currently regulatory targets are set at 30 days i.e. [x] = 30. Given that this is what we already report, we would prefer that the technical standards remain consistent with this.

Marking-to market and marking-to-model

ESMA is required to develop draft technical standards specifying the market conditions preventing marking-to-market and the criteria for using marking-to-model.

Insufficiently standardised for central clearing seems to heavily push towards marking to model.

Where market conditions prevent marking-to-market (market is inactive or the range of reasonable fair value estimates is significant and probabilities of various estimates cannot be reasonably assessed), financials and non-financials exceeding the clearing threshold shall use reliable and prudent marking-to-model. ESMA considers that the marking-to-model valuation technique should:

a. incorporate all factors that counterparties would consider in setting a price,

b. be consistent with accepted economic methodologies for pricing financial instruments,

c. be calibrated and tested for validity using prices from any observable current market transactions in the same financial instrument or based on any available observable market data,

d. be validated and monitored by a unit independent from the risk taking unit, and

e. be duly documented and approved by the board as frequently as necessary and at least annually.

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?

We have no comments to share.

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

We would bring to ESMA's attention that UCITS funds have specific requirements for the valuation of OTC derivatives, for example that a UCITS must be able to close out at any time at fair value. It is important that EMIR requirements not to conflict with UCITS requirements.

Reconciliation of non-cleared OTC derivative contracts

ESMA proposes the following:

- Financial and non-financial counterparties should agree in writing or in other equivalent electronic means with each of their counterparties on the terms of their portfolio reconciliation.
- Portfolio reconciliation should be performed by the counterparties to the OTC derivatives with each other, or by a qualified third party and should cover key trade terms that identify a particular derivative transaction.
- Portfolio reconciliation should be performed at least: (i) each business day when the counterparties have 300 or more OTC derivatives with each other; or (ii) at an appropriate time period based on the size and volatility of the OTC derivative portfolio of the counterparties with each other and at least once per quarter for portfolio of less than x derivative contract with a counterparty and at least once per week for portfolio between x and 300 derivative contracts with a counterparty for any other OTC derivative transaction not captured under (a) above.
- all counterparties should also have in place the necessary arrangements to timely resolve any discrepancy in a material term of a contract or in its valuation identified as part of the portfolio reconciliation.

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

While UBS agrees with the ESMA approach to increase the requirement in terms of portfolio size and frequency, we would bring to ESMA's attention that a more phased approach is preferable because there would be a reliance on the counterparty to also be able to support this operationally which may be a challenge for some smaller firms.

Portfolio compression

ESMA considers that:

- portfolio compression is a risk-reducing exercise which should be run on a regular basis.
- where multilateral portfolio compression services are proposed for a class of OTC derivatives, counterparties, especially when they already use services of that service provider, should include in the portfolio compression cycle all the OTC derivatives in their portfolio that are eligible for such cycle.
- financial counterparties and non-financial counterparties with at least 500 or more non centrally cleared derivative transactions should conduct at least twice a year a portfolio compression exercise for their full portfolio, or provide a reasonable and valid explanation to the relevant competent authority for not conducting such an exercise.
- financial and non-financial counterparties should terminate each of the fully offset derivative contract no later than the day following the execution of the fully offsetting derivative contract.

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

Whilst portfolio compression is desirable for operational risk management we do not believe it is appropriate to mandate compression especially where this would require the use of a third party commercial service provider. Most importantly, however, foreign exchange swaps, equity derivatives and commodities should be specifically excluded from any portfolio compression requirement due to the reasons outlined below.

Foreign Exchange Swaps should be excluded due to the short tenor of these trades, their non-standardized, bilateral nature and the considerable preparation time associated with the compression process, due to which there is minimal benefit to be gained from compression. Equity derivatives should be excluded as this market is broadly positional in nature, lacks product standardization and hence provides little opportunity for compression and netting. Finally the exclusion should apply to commodities as well as notional amounts are comparatively low.

We would furthermore argue that trade compression requirements to flatten offsetting trades need to recognize that some legal entities have segregated cell protection e.g. UK OEICs.

Lastly we would like to bring to ESMA's attention that asset managers whose clients choose to use several asset managers only see a part of a client's portfolio. They are hence not able to provide compression across the rest of the portfolio.

Dispute Resolution

Financial counterparties and non-financials should have:

– Detailed procedures and process in place for (i) identifying, recording, and monitoring disputes relating to the recognition, valuation of the contract or to the exchange of collateral between the two counterparties, at least recording the length of time for which the dispute remains outstanding, the counterparty, and the amount which is disputed; (ii) resolving disputes in a timely manner

– Procedures agreed by the counterparties to deal with disputes that are not resolved within 5 business days. This should include, but not be limited to, a combination of legal settlement, third party arbitration and/or a market polling mechanism.

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

While we agree that detailed procedures and process should be in place, we do not believe that resolving disputes in the proposed five day window is feasible. Time lines should be aligned with industry initiatives relating to dispute resolution and market polling.

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

In our view legal settlement and third party arbitration are available options but only usually required if all other resolution avenues have been pursued. The Market Polling Process is more typically used when other approaches to resolving disputes

have failed. ESMA's proposal should be consistent with current industry thinking on this topic.

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

UBS already submits such reports and has no issue to continue doing so.

Intragroup exemptions

With respect to uncleared trades, counterparties are required to undertake a timely, accurate and appropriately segregated exchange of collateral in order to minimize counterparty credit risk. A counterparty to an intragroup transaction, that is exempted from the clearing obligation, may also be exempted from the exchange of collateral requirement, provided certain conditions are met and the counterparty notifies the competent authority of its intention to use the exemption from the collateral requirement. Such counterparty is also required to publicly disclose information on the collateral requirement exemption.

ESMA requests views on the details of the intragroup OTC derivatives to be included in the notification to the competent authority as well as the details of information to be publicly disclosed. ESMA does not provide further information apart from the fact that it has only recently started the analysis.

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

As we are operating against a dynamic background where new classes of derivatives can be declared eligible for clearing by ESMA on a continuous basis, it is preferable, in our view, to make one application for a specified list of entities engaging in intragroup derivative transactions as well as a high level description of the classes of OTC derivatives they currently or intend to enter into. This would be less cumbersome than applying for an exemption whenever a new class of derivatives is declared eligible for clearing by ESMA.

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?

Consistent with the above approach, we would suggest that the entities which have intragroup relationships and which have been approved for exemption should be made public.

We do not advocate further information, for example number of trades, size of notional or RWA exposures as the most common purpose of intragroup transactions is to allow for netting at a parent level where true net exposures are calculated and elements of OTC derivatives and their underlying hedges can be brought together. Splitting out elements of the relationships will only give partial, potentially one-sided elements of the exposure which could be misleading and is not the way such transactions are managed within banking groups.

III.II. CCP REQUIREMENTS
ACCESS TO A VENUE OF EXECUTION (ARTICLE 8A)

According to Article 8a of EMIR, access to a CCP by a venue of execution can only be granted if such access would not require interoperability or threaten the smooth and orderly functioning of markets in particular due to liquidity fragmentation. In this context, ESMA is required to specify through draft RTS the notion of liquidity fragmentation.

Q23: What are your views on the notion of liquidity fragmentation?

We understand ESMA's question to refer to Derivatives only as Cash Equities already is fully interoperable.

The model envisioned in Article 8a is one where multiple venues of execution can match the same instrument and deposit each trade into the single CCP netting pool of the core open interest of that instrument from the incumbent venue of

execution. It is unclear to us what ESMA considers to be a "fragmentation of liquidity" in the context of clearing as in our view, this would only be relevant at the trading rather than the clearing layer.

ORGANISATIONAL REQUIREMENTS (ARTICLE 24)

Under Article 24 of EMIR, ESMA is required to draft regulatory technical standards specifying details on: governance arrangements; compliance policy and procedures; information technology systems; reporting lines; remuneration policy; disclosure of rules and governance arrangements and admission criteria; audits.

CCP requirement on governance arrangements are to include:

(a) They should be designed in a way as to promote sound and prudent management and thereby support financial stability and foster fair and efficient markets.

(b) The CCP organisational structure should be well-documented and include the policies, procedures and processes by which the board and senior management operate.

ESMA furthermore considers that while the board of a CCP assumes the final responsibility and accountability for the CCP's actions, a CCP should name dedicated chief risk officer, chief technology officer and chief compliance officer and heads of any other function it considers relevant. Where a CCP is part of a larger organisation it should duly consider any implications of the larger organisation for its own governance arrangements including whether it has the necessary level of independence to meet its regulatory commitments as a distinct legal entity and that this independence will not be compromised by the group structure or by board members also being members of the board of other parts of the same group. In particular, such CCP should consider specific procedures for preventing and managing conflicts of interest including with respect to outsourcing arrangements.

Q24: What are your views on the possible requirements that CCP governance arrangements should specify? In particular, what is your view on the need to clearly name a chief risk officer, a chief technology officer and a chief compliance officer?

In our view, it is important that the governance of CCPs clearly addresses the inherent conflict of interest of the CCP as a profit-making organisation versus providing sound risk management required of a central clearer.

We would argue that the naming of CROs, CTOs and CCOs although welcome, does not materially change the governance structure. This is because the Board is ultimately responsible and empowered to over-rule such persons as well as any internal committees. To that extent, a possible approach would be to elect such CROs, CTOs and CCOs onto the Board with full voting rights.

Q25: Are potential conflicts of interests inherent to the organisation of CCPs appropriately addressed?

We refer to our response in Q24.

Q26: Do the reporting lines – as required – appropriately complement the organisation of the CCP so as to promote its sound and prudent management?

The important component here will be to split the reporting structure where the CCP is part of a larger Exchange organization. The independent function of the LCH acting as a clearing house for Euronext is an example of the outsource model that would be preferable to the vertical silo model that exists for Eurex.

Q27: Do the criteria to be applied in the CCP remuneration policy promote sound and prudent risk management? Which additional criteria should be applied, in particular for risk managers, senior management and board members?

As a more general comment,, we would emphasize our view that if the overriding principles of the CCP function are to provide financial stability, fairness and efficiency, then it would seem that this is difficult to deliver in the framework of the "for profit" model.

Q28: What are your views on the possible organisational requirements described above? What are the potential costs involved for implementing such requirements?

Regarding the principle of "efficiency", there are many stakeholders in the complete model from end user to CCP. It is critical that the design of the CCP structure is built for a scalable, robust solution for the benefit of the clearing members towards which the CCP owes a duty of care and the wider user base. The organizational requirements that the CCP will need to follow, as set out in the Paper, are appropriate and necessary. These requirements as well as ongoing monitoring of the CCP will be expensive to implement.

Q29: Should a principle of full disclosure to the public of all information be necessary to be able to understand whether and how the CCP meets its legal obligations be included in the RTS? If yes, which should be the exceptions of such disclosure requirements? Has the information CCP should disclose to clearing members been appropriately identified? Should clients, when known by the CCP, receive the same level of information?

Yes, there should be a principle of full disclosure to the public. Disclosure information should include notice of any changes to each counterparty to allow debate and implementation changes for clearing members and vendors including e.g. margin models, eligible collateral and haircuts. In addition to the listed requirements, there should be clarity on the specific processes regarding any default

procedures, especially for the different segregation options. In our view, clients should receive the same level of information as clearing members because it is the clients who select which CCP they wish to use.

RECORD KEEPING (ARTICLE 27)

ESMA considers that CCPs should maintain transaction, position and business records.

Regarding transaction records, ESMA considers that

(i) CCPs should maintain records of all contracts cleared and should ensure that their records include all information necessary to conduct a comprehensive and accurate reconstruction of the clearing process for each contract and that each contract record is univocally identifiable and searchable by every field indicated in letter under (ii),

(ii) For every contract received for clearing, a CCP should immediately make a record at a minimum of:

- the unit price (and price notation), the quantity (and quantity notation);
- the clearing capacity, which identifies whether the contract was a buy or sell from the perspective of the CCP recording;
- the instrument identification the identification of the clearing member and of the client, if known to the CCP, and in case of a give-up, the identification of the party that transferred the contract;
- the identification of the venue where the contract was concluded (if OTC such indication will apply);
- the date and time of interposition of the CCP in the contract;
- the date and time of termination of the contract;
- the terms and modality of settlement;
- the date and time of settlement or of buy-in of the contract;
- and to the extent applicable: day and time at which the contract was concluded; identification of original terms and parties of any contract cleared; identification of the interoperable CCP clearing one leg of the transaction.

Regarding positions, ESMA considers that CCPs should keep the following records:

a. They should maintain records of positions held by each clearing member separately for each account kept in accordance with Article 37 of EMIR and should ensure that these records include all information necessary to conduct a comprehensive and accurate reconstruction of the transactions that established the position and that each record is identifiable and searchable at a mini-mum by each of the field specified in letter b. below.

b. CCPs, at the end of every day and in relation to each position, should make a record, at a mini-mum of the following details, to the extent they are applicable to the position in question:
- the identification of the clearing member, of the client, if known to the CCP, and of the interoperable CCP maintaining such position, where applicable;
- the position identification as "long" or "short";
- the daily calculation of the value of the position with records of the prices at which the contracts are valued, and of any other relevant information;
- the amounts of margins, default fund contributions and other financial resources, distinguished by pre-funded and non-pre-funded, called by the CCP at the end of day and intra-day, with respect to each single clearing member and client account.

Regarding business records, ESMA considers that CCPs should maintain adequate and orderly records of activities related to its business and internal organisation. Those records should be made each time a material change in the relevant documents occurs. CCPs should keep:

a. organisational charts for the board and relevant committees, clearing unit, risk management unit, and all other relevant units or divisions;
b. identities of the shareholders or members, whether direct or indirect, natural or legal persons, that have qualifying holdings and the amounts of those holdings;
c. documents attesting the policies, procedures and processes required under the relevant organisational requirements;
d. minutes of board meetings, board sub-committees, senior management committees;
e. minutes of meetings of the risk committee;

f. minutes of consultation groups with clearing members and clients, if any
g. internal and external audit, risk management, compliance, and consultant reports
h. business continuity policy and disaster recovery plan;
i. liquidity plan and the daily liquidity reports;
j. records reflecting all assets and liabilities, capital accounts as required by EMIR
k. complaints received, with information on the complainant's name, address, and account number; the date the complaint was received; the name of all persons identified in the complaint; a description of the nature of the complaint; the disposition of the complaint, and the date the complaint was resolved;
l. records of any interruption of services or dysfunction, including a detailed report on the timing, effects and remedial actions;
m. records of the results of the back and stress tests preformed;
n. written communications with competent authorities;
o. legal opinions received in accordance with RTS on organisational requirements;
p. where applicable, documentation on CCP interoperability arrangements

The records should be retained in a medium that allows the storage of information in a format accessible for future reference, and in such a form and manner that i) it is possible for the competent authorities to access the records readily and to reconstitute each key stage of the processing involved; ii) it is possible to record, trace and retrieve the original content of a record before any corrections or other amendments; and iii) it is not possible for the records to be manipulated or altered.

All records required to be kept by CCPs should be open to inspection by the competent authority. The CCP should name the relevant person or persons that can, without delay, explain the content of the records maintained.

Q30: What are your views on the possible records CCPs might be required to maintain?

We would query if a 10 year history for position and transaction data is effectively required.

Q31: What are your view on the modality for maintaining and making available the above records? How does the modality of maintaining and making available the records impact the costs of record keeping?

We have no views as to the modality of making such records available. We would, however, question to what extent the above records would already be recorded under the TR requirements and believe that any duplication should be avoided to avoid unnecessary costs.

BUSINESS CONTINUITY (ARTICLE 32)

Q32: What are your views on the possible requirements for the business continuity and disaster recovery plan and in particular on the requirements for the secondary site? Would it be appropriate to mandate the establishment of a third processing site, at least when the conditions described above apply? What are the potential costs and time necessary for the establishment of a third processing site and for immediate access to a secondary business site?

At a high level, we believe that the requirements stated by ESMA are sound and appropriate as the primary factors to be considered when defining and implementing a disaster recovery plan. However, it is worth asking the CCP to consider along with its major market participants what timing changes could be implemented under certain disaster scenarios. For example, if the CCP itself has been unavailable for clearing for a period of the day it is worth considering extending the CCP clearing hours to later in the day to allow any backlogs of uncleared trades to be successfully processed through to the CCP.

As a market participant, exposed only to certain functions of a CCP and other aspects of market infrastructure, it is difficult to provide accurate commentary on whether a third processing site is necessary. It is in our view sensible not to mandate a third processing site since a mandatory third site could be imposing an unsustainable cost base on market participants to cover a risk which is highly unlikely to occur. The necessity for a third processing site should be driven by an

assessment of the impact and likelihood of the primary and secondary sites being inoperative at the same time versus the cost of implementing and maintaining a third site.

When considering a secondary business continuity side, we believe that a range of potential requirements needs to be considered such as (i) distance from primary site and the vulnerability of the secondary site to be impacted by the same disasters, (ii) secondary site accessibility, especially for support staff in a disaster event as well as available options for travelling to the secondary site, (iii) similarities in infrastructure and suppliers (buildings, power supply, telecommunications, etc) between primary and secondary site as it could mean the secondary site is also impacted by the failure of the primary site infrastructure and/or supplier.

Q33: Is the 2 hours maximum recovery time for critical functions a proportionate requirement? What are the potential costs associated with that requirement?

The recovery time will depend on the individual function or service. Some CCP services are deemed mission critical (e.g. ability to clear trades intra-day, real-time credit checking) which would need to have the fastest recovery times. There will be other services which are less critical for mitigating systemic risk (e.g. billing) which could have slower recovery times and not impact market participants and/or stability severely. A review of historic market stressed periods together with specific CCP disaster scenarios would provide good practical evidence for which services are deemed critical and therefore need the fastest recovery times. The costs associated with creating a recovery plan can be considerable especially when such services are used infrequently, therefore a detailed cost/benefit analysis is necessary to understand the costs so they can be compared with the risk that they are mitigating and crucially the likelihood of a disaster occurring. The impact of a particular service being unavailable may be catastrophic but the decision to implement a full recovery plan should be considered against the likelihood of the disaster occurring. A way of mitigating or offsetting high costs could be for CCP to use their disaster recovery solutions to run their production services (it also allows frequent practice of conducting a failover). Another potential option to be considered for disaster

recovery planning at individual CCPs is whether market participants are able to clear at other CCPs (inter-operability). This could be one of the most cost effective disaster recovery plans for a particular market.

MARGINS (ARTICLE 39)

Q34: Are the criteria outlined above appropriate to ensure that the adequate percentage above 99 per cent is applied in CCP's margin models? Should a criteria based approach be complemented by an approach based on fixed percentages? If so, which percentages should be mandated and for which instruments?

For the definition of the appropriate confidence interval, our preference is a criteria based approach specifying minimum standards. In addition to the criteria already outlined by ESMA, the distribution of historical price movements/changes should be an additional key factor to be considered.

We prefer this approach as it will make the process of making appropriate changes as market conditions and product features change less cumbersome. Internal governance controls and sign-off procedures should in our view be sufficient to allow for such changes.

As a general comment, we would emphasize our view that margins are the first line of defense and is synonymous with the "user-pays" principle. To this end, care should be taken so as to not be overly-reliant on other risk controls to minimize margins. As an example, "super-margining" a clearing member outside of the product margins effectively creates a funding mechanism whereby clearing members are subsidizing clients/end-users increased leverage.

Q35: Taking into account both the avoidance of procyclicality effects and the need to ensure a balance distribution of the financial resources at the CCP disposal, what it is in your view the preferred option for the calculation of the lookback period.

We prefer Option C where initial margins are calculated on the basis of both stable and stress market conditions, but where both are equally weighted. However, this needs to be implemented in conjunction with appropriate Confidence Intervals.

Alternatives would be to consider an approach between Option B and C as current practices of Option B places too little weight to observations in the past. Also worth considering in our view is an Expected Tail Loss as this avoids the pitfalls of specifying a precise point at the required Confidence Interval where the next worse observations might be materially different.

Q36: Is in your view the approach described above for the calculation of the liquidation period the appropriate one? Should a table with the exact number of days be included in the technical standards? Should other criteria for determining the liquidation period be considered?

ESMA should specify minimum standards for the CCP to determine appropriate liquidation periods.

A key issue which needs to be addressed is that estimation of liquidation times during the default management process must be in the context of a stressed market environment. This means that any references to current liquidity/volume must be appropriately discounted.

Q37: Is procyclicality duly taken into account in the definition of the margin requirements?

We have no comments to provide.

DEFAULT FUND (ARTICLE 40)

Q38. What is your view of the elements to be included in the framework for the definition of extreme but plausible market conditions?

While we believe that the elements to be included in the framework are reasonable, we would have two comments to add. First it is a common misconception that Exchange Traded Products are more "liquid" and hence easier to manage during a default. Second with the focus on central-clearing, CCPs are the new "too-big-to-fail" entities. Extreme conditions should consider the impact of a CCP failing and the associated market impact.

LIQUIDITY RISK CONTROLS (ARTICLE 41A)

With reference to liquidity risk controls requirements, ESMA is required to develop technical standards specifying the framework for managing liquidity risk. ESMA will therefore have a quite broad mandate with respect to liquidity risk controls.

Q39: Do you believe that the elements outlined above would rightly outline the framework for managing CCPs' liquidity risk?

Yes. However, it in our view important to further distinguish between countries that may share the same currency such as the Euro. CDS spreads and credit ratings (internal and external) should both be taken into consideration in establishing a low credit risk entity.

Q40: Do you consider that the liquid financial resources have been rightly identified? Should ESMA consider other type of assets, such as time deposits or money market funds? If so, please provide evidences of their liquidity and minimum market and credit risk.

We believe that money market funds should not be considered. We furthermore believe that there is no reason to consider time deposits if the concern is to address liquidity.

Q41: Should the CCP maintain a minimum amount of liquid assets in cash? If so, how this minimum should be calculated?

Yes, we believe CCPs should maintain a minimum amount of liquid assets in cash corresponding to 2 x the Initial Margin of the largest clearing member.

DEFAULT WATERFALL (ARTICLE 42)

Under the RTS for the default waterfall, ESMA is required to specify the methodology for calculation and maintenance of CCPs own resources to be used in a default situation before the resources of the non-defaulting clearing members can be mutualised, i.e. so called "skin in the game". For the determination of such an amount, ESMA is considering the following two options:

Option A: [X%] of the average amount of the margins and default fund contributions collected by the CCP over a one year period (excluding margins posted by interoperable CCPs);

Option B: [X%] of the CCPs total capital resources as requested in accordance to Article 12 of EMIR, whose details would need to be specified through RTS to be developed by EBA.

Q42: What is your preferred option for the determination of the quantum of dedicated own resources of CCPs in the default waterfall? What is the appropriate percentage for the chosen option? Should in option a, the margins or the default fund have a different weight, if so how? Should different criteria or a combination of the above criteria be considered?

We prefer Option A. The CCP's contribution into the default fund should be x% of margins. As a CCP is a profit-making entity, it should also have considerable resources as a back-stop to manage defaults of clearing members. A substantial portion of these resources should be from its own capital. More specifically the

amount of capital which a CCP should have at stake in the waterfall should be sufficient to cover the first default i.e. of the single largest member.

Q43: What should be the appropriate frequency of calculation and adaptation of the skin in the game?

It should coincide with the standard frequency of guaranty fund replenishments, which we understand to be typically monthly. In the same way that banks are required to manage their balance sheet to ensure capital does not fall below regulatory minimums, so too should CCPs.

COLLATERAL REQUIREMENTS (ARTICLE 43)

Under the RTS for collateral ESMA is required to define the type of collateral that can be considered highly liquid as well as conditions under which commercial bank guarantees may be accepted as collateral.

Q44: Do you consider that financial instruments which are highly liquid have been rightly identified? Should ESMA consider other elements in defining highly liquid collateral in respect of cash of financial instruments? Do you consider that the bank guarantees or gold which is highly liquid has been rightly identified? Should ESMA consider other elements in defining highly liquid collateral in respect of bank guarantees or gold?

In the case of financial instruments, the liquidity of financial instruments or trade-able volume of such securities in the marketplace should also be taken into consideration. This impacts the ability for the CCP to offload substantial amounts of a specific issue/tenor/maturity. We would furthermore welcome clarity on the definition of "low market risk" stated in 120 (2) (ii). In regards to point 120.2.(v) – it is our view that price information should be available daily including intraday. In the case of commercial bank guarantees, the credit risk assessment should also take into account credit spreads and rating (internal as well as external).

From a buy side perspective we would advocate that the rating eligibility criteria is extended to include highly liquid corporate bonds to a rating of BBB. We believe

that such an extension should be considered as long as the other criteria such as diversification, pricing and credit spreads are maintained.

Q45: In respect of the proposed criteria regarding a CCP not accepting as collateral financial instruments issued by the clearing member seeking to lodge those financial instruments, is it appropriate to accept covered bonds as collateral issued by the clearing member?

It would be appropriate to evaluate the legal framework under which these bonds are issued, the underlying security provided as cover and the impact of these issues on trading/liquidity.

Q46: Do you consider that the proposed criteria regarding the currency of cash, financial instruments or bank guarantees accepted by a CCP have been rightly identified in the context of defining highly liquid collateral? Should ESMA consider other elements in defining the currency of cash, financial instruments or bank guarantees accepted by a CCP as collateral? Please justify your answer.

We refer to our comments in Q44.

Q47: Do you consider that the elements outlined above would rightly outline the framework for determining haircuts? Should ESMA consider other elements?

Yes, we consider the elements rightly outline the framework. ESMA should also consider issuance size and liquidity of such financial instruments i.e. the trade-able volume of such securities in the marketplace.

The level and volatility of the interest rate should also be included.

Q48: Do you believe that the elements outlined above would rightly outline the framework for assessing the adequacy of its haircuts? Should ESMA consider other elements?

We refer to our response in Q47.

Q49: Do you consider that the elements outlined above would rightly outline the framework for determining concentration limits? Should ESMA consider other elements?

We refer to our response in Q47 in that ESMA should consider issuance size and liquidity of such financial instruments.

Furthermore currency and country should be taken into account.

Q50: Should a CCP require that a minimum percentage of collateral received from a clearing member is provided in the form of cash? If yes, what factors should ESMA take into account in defining that minimum percentage? What would be the potential costs of that requirement?

We question whether ESMA should require CCPs to mandate a minimum percentage of collateral in the form of cash. In our view, CCPs should be able to define this percentage themselves by considering liquidity factors as appropriate. The aim should be to strike the right balance between maximizing liquidity and ensuring that the cash collateral requirements extended to buy-side participants (who are fully invested) are economically viable for the latter.

INVESTMENT POLICY (ARTICLE 44)

Q51: Do you consider that financial instruments and cash equivalent financial instruments which are highly liquid with minimal market and credit risk have been rightly identified? Should ESMA consider other elements in defining highly liquid financial instruments with minimal market and credit risk? What should be the timeframe for the maximum average duration of debt instrument investments?

We refer to our earlier comments in that CCPs should also consider issuance size and liquidity of such financial instruments i.e. trade-able volume of such securities in the marketplace. ESMA should also consider credit spreads in assessing credit risk.

Furthermore it would be beneficial to define what is meant by "low market risk". Cash investments such as term deposit and reverse-repos (i.e. invesments which are not trade-able and cannot be liquidated daily) should not have a tenor longer than the expected liquidation period used in determining margins.

Q52: Do you think there should be limits on the amount of cash placed on an unsecured basis?

Yes, but in conjunction with issuer limits.

Q53: Do you consider that CCP should be allowed to invest in derivatives for hedging purposes? If so, under which conditions and limitations.

No, we do not believe so.

Q54: Do you consider that the proposed criteria regarding the currency of financial instruments in which a CCP invests has been rightly identified in the context of defining highly liquid financial instruments with minimal market and credit risk? Should ESMA consider other elements in defining the currency of highly liquid financial instruments with minimal market and credit risk? Please justify your answer.

Yes, we believe they have been rightly identified.

Q55: Do you consider that the elements outlined above would rightly outline the framework for determining the highly secured arrangements in respect of which financial instruments lodged by clearing members should be deposited? Should ESMA consider other elements? Please justify your answer.

In respect of credit institutions, this should be in pure custody form only and ideally segregated from other clients of the credit institution.

Q56: Do you consider that the elements outlined above would rightly outline the appropriate framework for determining concentration limits? Should ESMA consider other elements? Please justify your answer.

Yes, they do.

REVIEW OF MODELS, STRESS TESTING AND BACK TESTING (ARTICLE 46)

Q57: What are your views on the definitions of back and stress testing?

We refer to our earlier comments.

Model Validation

Q58: What are your views on the possible requirements for a CCP's validation process?

A CCP's validation process should be audited and signed off by the Board. Any exceptions or recommendations outside of the testing should be clearly documented and explained.

Q59: What are your views on the possible back testing requirements?

We have no comments to offer.

Q60: Would it be appropriate to mandate the disclosure of back testing results and analysis to clients if they request to see such information?

We have no comments to offer.

Q61: Should the time horizons for back tests specified under 144(e) be more granular? If so, what should the minimum time horizon be? Should this be different for different classes of financial instruments?

We have no comments to offer.

Stress Tests

Q62: What are your views on the possible stress testing requirements?

We have no comments to offer.

Q63: Would it be appropriate to mandate the disclosure of stress testing results and analysis to clients if they request to see such information?

We have no comments to offer.

Q64: What are your views on the possible requirements for reverse stress tests? And what impact do you think such requirements would have on industry?

We support the requirements for reverse stress tests as it will improve risk management of the CCP.

Testing results and Involvement of Parties in Tests

Q65: Should there be any other parties involved in the definition and review of tests? Please justify your answer and explain the extent to which suggested parties should be involved?

CCPs should be allowed to appoint independent advisors or consultants to review such results as clients may be conflicted to provide a fair assessment or critique of the tests.

Q66: Should the testing of default procedures involve a simulation process?

Yes. However, considering that many banks/brokers are concurrent members across various CCPs, it should be obligatory on the CCP industry to co-ordinate internally

to ensure members are not forced to participate in multiple default management processes at the same time.

Frequency of Tests

Q67: Are the frequencies specified above appropriate? If no, please justify your answer.

Yes, we believe them to be appropriate.

Information to be publicly disclosed

Q68: In your view what key information regarding CCP risk management models and assumptions adopted to perform stress tests should be publicly disclosed?

We have no comments to offer.

III. III. TRADE REPOSITORIES

ESMA considers the following elements when drafting the regulatory technical standards (RTS) on details and type of reporting: (i) purpose of reporting, (ii) content of reporting (parties, contract type, details on transaction, risk mitigation and clearing, specific derivative classes), (iii) level of granularity.

In developing draft RTS format on format and frequency of reporting, ESMA considers: (i) the actual fields in each report, (ii) standard codes for the identification of e.g. contracts, trades and counterparties/clients.

REPORTING OBLIGATION (ARTICLE 6/7)

Q69: What is your view on the need to ensure consistency between different transaction reporting mechanisms and the best ways to address it, having in mind any specific items to be reported where particular challenges could be anticipated?

Maintaining consistency between different transaction reporting mechanisms is essential to ensure costs of regulatory adherence are kept to a minimum. The approach outlined by ESMA, by ensuring trade repositories are authorised by EEA regulators before taking on their responsibilities and stipulating required fields (incorporating trade, transaction and wider Exchange reporting requirements) appears sensible to us.

We advocate the importance of harmonizing reporting mechanisms between EMIR and MiFID II to avoid the duplication of reporting capabilities as well as across regulators and jurisdictions in particular in regards to existing ETD practices.

Q70: Are the possible fields included in the attached table, under Parties to the Contract, sufficient to accurately identify counterparties for the purposes listed above? What other fields or formats could be considered?

Overall we believe that the fields outlines in Annex II Tables 1 & 2 appear to be comprehensive. They capture all transaction reporting fields aside from a cancellation field to indicate if the trade is cancelling a previously submitted trade.

We have the following specific comments to offer:

Table 1 (Counterparty Data) - "Financial Entity/Counterparty" Field: we would welcome if the definitions of "financial entity/counterparty" were aligned between Dodd-Frank and EMIR. This adds another layer of reference data for counterparty classification to be maintained

Table 1 (Counterparty Data) "Beneficiary / Trade with Non-EEA Counterparty / Directly Linked to Commercial Activity or Treasury Financing / Clearing Threshold" Fields: We would welcome alignment with Dodd-Frank Title VII as the industry has spent considerable time developing the solution to report data fields.

Table 2 (Common Data) "Type of Venue of Execution" Field (Regulated Market; Multilateral Trading Facility, Organised Trading Facility, Systemic Internaliser, OTC): we note that these are new fields not introduced in Dodd-Frank Title VII. We would welcome an alignment of the "Type of Venue of Executions" definition of execution venues with the DFA. We would query the practical implications resulting from the reporting process, specifically if the execution venues would report on our behalf and how would we connect to all these different venues.

Table 2 (Common Data) "Price Multiplier" Field: we would welcome clarity if this relates to ETD.

Table 2 (Common Data) "Master Agreement type / Master Agreement Date" Fields: we would bring to ESMA's attention that Reporting Master Agreement Data cannot be easily provided. To be able to report this data along with individual trades will require substantial IT investments.

Table 2 (Common Data) "Clearing Timestamp" Field: it is our understanding that this will be reported by CCPs. We would welcome clarification/confirmation.

Common Data may be reported by the two counterparties separately or may be reported only once where one counterparty reports on behalf of the other counterparty. We would question what the reporting party determination is and would welcome consistency with the U.S. on this point. We would stress our concern that there is potential for double-counting if two parties report the same transaction, especially where they have two different transaction IDs.

Beneficiaries

Q71: How should beneficiaries be identified for the purpose of reporting to a TR, notably in the case of long chains of beneficiaries?

Identification of counterparties: The field identified within the table 1 to identify counterparties appear comprehensive. We would, however, question what value the corporate sector of the counterparty and link to commercial activity requirements for each counterparty is to trade repositories or regulators, as this is subject to some subjectivity (e.g. certain bankassurance groups have both insurance and banking arms so placing them in a banking or insurance group might be somewhat arbitrary).

Identification of economic beneficiary: We oppose the identification of the economic beneficiary for a number of reasons. Not only is the economic beneficiary very difficult to prove in practice, in particular where natural persons are involved, it is also not consistent with the reporting infrastructure the industry is building to support Dodd-Frank Title VII. We would furthermore stress the fact that where counterparties would be required to disclose their own clients to us, the bank-to-bank model common in continental Europe could no longer be maintained. We would also like to stress that the focus of trade repositories is on understanding systemic risk. The identity of a natural person is likely to be of no benefit in this context.

Other practical difficulties of obtaining details on both the counterparty and ultimate economic beneficiary are the following:

i) Firms located outside the EU may be restricted by local law from passing on client / beneficiary details
ii) Data privacy concerns where client ID's are transmitted on an international basis are likely to arise
iii) Certain investment firms operate on a global basis and currently there are no single client identifier which covers all different country reporting norms such as, for example, passport number, national insurance number, citizen card.

iv) Details of underlying client details might not be passed across to brokers / fund managers due to commercial sensitivities, making it impossible to populate all requirements

v) Rules covering KYC might need to be enhanced to ensure all elements set out in Table 1 are captured as part of the OnBoarding process (for example "financial / non financial, corporate sector classifications are not currently stipulated).

Coding

ESMA is required to develop ITS specifying the formats that need to be used in the reporting of trade information to TRs, and consequently considers the widest usage of coding as possible. Codes are being considered for three types of identification: counterparty, product and trade.

In relation to counterparties, two sorts of codes may be considered: if a legal person, a legal entity identifier (LEI); if a natural person, an easily and widely available unique identifier. Under the MiFID TR system, such identifier coincides with the client id assigned by the intermediary but does not comply with the principle of universality as it does not allow for the identification of the same individual reported by two different intermediaries.

In relation to products, ESMA considers that the following should be reported to a TR: product taxonomy, product ID and underlying. On taxonomy, ESMA will take subsidiary action if the market does not develop an adequate solution for TR reporting purposes. On product codes, ESMA does not take a view on the specific providers involved in the development of a unique product. It is following market initiatives and defined clear principles for coding, two of which are open access and global reach, which are being development at FSB level and supported by G20 (with respect to the LEI project).

Q72: What are the main challenges and possible solutions associated to counterparty codes? Do you consider that a better identifier than a client code could be used for the purpose of identifying individuals?

We refer to our response to Q71. We support the use of counterparty codes while advocating for some flexibility on the detail used to submit client information.

We would reemphasize our concerns with the concept of identifying the economic beneficiary specifically as they relate to data confidentiality and bank secrecy.

Any kind of reference data or IDs needs to be a global standard that is harmonized with the CFTC, HKMA and other regulators, namely the Legal Entity Identifier (LEI).

Q73: What taxonomy and codes should be used for identifying derivatives products when reporting to TRs, particularly as regards commodities or other assets for which ISIN cannot be used? In which circumstances should baskets be flagged as such, or should their composition be identified as well and how? Is there any particular aspect to be considered as regards a possible UPI?

Taxonomy and codes should be a global standard, aligned with industry initiatives relating to UPI. Dodd-Frank commentary has noted that the UPI may not cover 5-20% of the population. We assume that "baskets" refer to whether we report at a product level or include the underlying (which is required under Dodd Frank). The industry preference is to report at a product level. If required to report the underlying, we would prefer a common approach vs. Dodd-Frank and other jurisdictions.

Details on the transaction

To effectively match counterparties to trade ESMA considers that where those trades are reported separately by each counterparty, a trade ID should be reported with each counterparty to allow for the matching of each side of the transaction. Such a code could be agreed bilaterally and assigned by counterparties, or generated by the trading platform. As noted, consistent and unique coding systems

for these trade IDs are crucial to reduce reporting costs and to increase the efficiency of reporting and analysis by ensuring different TRs are able to accurately match transactions within their systems.

Q74: How complex would be for counterparties to agree on a trade ID to be communicated to the TR for bilaterally executed transactions? If such a procedure is unfeasible, what would the best solution be to generate the trade ID?

We believe this is covered by the USI initiative. Again this needs to be in the same format and usage rules/generation rules as Dodd-Frank.

Pricing and fees

ESMA considers three essential elements within the reporting obligation under EMIR that will be useful to authorities in understanding the price at which derivatives are traded: (a) price/rate/spread; (b) price multiplier; and (c) up-front payment. Other elements could be taken into account, including on fee-related elements and other sub-sets of pricing.

ESMA considers that it may be of regulatory interest for authorities to understand the extent to which the trading price differs from market fair value as a result of fees being incorporated into a price by a broker when trading with a client. This would allow regulators to understand the market fair value of trades and the impact on fees of pricing for different derivatives products.

Q75: Would information about fees incorporated into pricing of trades be feasible to extract, in your view?

As a general comment we would emphasize our view that this should be aligned with Dodd-Frank, which requires reporting of pricing and fees only if price-impacting.

In regards to fee information, it is important to note that OTC products ordinarily are quoted in a way that the spread reflects the fees firms are charging within the price quoted. We do not consider an abstraction to be feasible.

Risk Mitigation and Clearing

ESMA is considering a number of fields to be reported.

a. a timestamp on the time of reporting to the TR;
b. the type of platform where the trade was executed;
c. whether confirmation has taken place on the transaction and, if so, whether it was by electronic means;
d. whether the exposure of counterparties to the trade is collateralised;
e. whether there is an obligation to clear, whether the trade was cleared and, if cleared, when the trade was novated for clearing and by which CCP;
f. whether the trade qualifies as intra-group for the application of the exemption on intra-group trades.

Q76: What is your view of the granularity level of the information to be requested under these fields and in particular the format as suggested in the attached table?

The granularity of the information requests seems appropriate. We note that the suggested information is in line with Dodd-Frank except for points noted in Q70. Further details on conventions obviously still need to be worked out such as if prices are to be quoted in pounds or pence and which international time zone should trade times be quoted.

Specific asset classes

Q77: Are the elements in the attached table appropriate in number and scope for each of these classes? Would there be any additional class-specific elements that should be considered, particularly as regards credit, equity and commodity derivatives? As regards format, comments are welcome on the possible codes listed in the table.

We underline the importance of alignment with Dodd-Frank, which has very specific inclusions/exclusions for commodities, not just in attributes but specific products.

Additional Points

ESMA considers a phased-in approach to capture data on exposures and collateral to take into account the IT, operational and financial challenges involved and deems that data on (i) current exposures of a given counterparty at the bilateral portfolio level and (ii) collateral are important to be able to assess counterparty risk.

Q78: Given that daily mark-to-market valuations are required to be calculated by counterparties under [Article 6/8] of EMIR, how complex would it be to report data on exposures and how could this be made possible, particularly in the case of bilateral trades, and in which implementation timeline? Would the same arguments also apply to the reporting of collateral?

We note that the daily mark requirement is consistent with Dodd-Frank. We would highlight the fact that collateral reporting was removed from Dodd-Frank as there was large overhead to firms in including it.

Reporting by Third Parties

According to ESMA reporting to TRs may be undertaken by third parties, as long as such third parties are carefully selected by counterparties to ensure they are providing accurate and timely information to TRs. Third parties need to guarantee protection of the data and compliance with the reporting obligation the same way the counterparty appointing them is required to. ESMA may request the competent authority of a counterparty to take action in relation to the use of a third party reporting entity which is not able to ensure that counterparties duly comply with their reporting obligations under EMIR and/or do not enable TRs to perform their duties. In extreme cases, ESMA should be able to prevent a TR under its supervision to accept reporting by third parties that may jeopardize the accuracy of the data held in the TR.

Q79: Do you agree with this proposed approach? What are in your view the main challenges in third party reporting and the best ways to address them?

We underline the importance of alignment with Dodd-Frank, which differentiates between registered entities (SEF/DCM/DCO) versus third-party service providers (e.g. Markitwire). We would welcome further clarity from ESMA as to what third parties are permitted.

APPLICATION FOR REGISTRATION (ARTICLE 52)

ESMA gives details on its expectations on the following elements as part of the application process: (i) ownership, (ii) organisational structure, governance and compliance, (ii) staffing and compensation, (iv) financial resources, (v) conflicts of interest, (vi) resources and procedures, (vii) access and transparency, (viii) operational reliability, (ix) recordkeeping and (x) data availability.

In defining the format of the application for registration of TRs, ESMA believes that an application for registration shall be provided in an instrument which (a) stores information in a way accessible for future reference; and (b) allows the unchanged reproduction of the information held.

Q80: Do you envisage any issues in providing the information / documentation as outlined above? In particular:
a) what would the appropriate timeline over which ESMA should be requesting business plans (e.g. 1, 3, 5 years?)

b) what would the appropriate and prudent length of time for which a TR must have sufficient financial resources enabling it to cover its operating costs (e.g. 6 months / 1 year)?

The trade repository authorisation information being requested appears appropriate aside from staffing & compensation. Providing specific remuneration details of employees who are not directors or significant management would be inappropriate. In regards to a) we believe a three year business plan to be

appropriate. For b) we believe a six month resource funding requirement to be sufficient for business to be transferred across to other competitors or alternative trade repositories established.

Q81: What is your view on these concerns and the ways proposed to address them? Would there be any other concerns to be addressed under the application for registration and tools that could be used?

We have no comments to provide.

TRANSPARENCY AND DATA AVAILABILITY (ARTICLE 67)

When considering technical standards defining the scope of the TR-held data to which authorities and the public will have access to, ESMA considers the following key elements:

a. granularity of data to be disclosed per type of recipient: (i) for the public; (ii) for each relevant authority;
b. how information should be disclosed and organised;
c. the means to receive this
d. frequency of disclosure to both the public and to the different authorities; and
e. level of aggregation to be considered in the public disclosure or depending of the receiving authority.

Q82: What level of aggregation should be considered for data being disclosed to the public?

We have no comments to offer

Q83: What should the frequency of public disclosure be (weekly? monthly?); and should it vary depending on the class of derivatives or liquidity impact concerns; if yes, how?

We have no comments to offer.