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 BSBV 48/2012 31.7.2012

 Dr.Egger/Ob

**ESMA- Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories**

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on ESMA- Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositoriesand would like to submit the following position:

In general we believe that a phased-in implementation of both the clearing and transaction reporting obligations will reduce risks and promote a smoother implementation. The implementation of both the clearing and transaction reporting obligation should be phased-in at an appropriate future date.

**Ad Annex II, Chapter II (Indirect Clearing Arrangements)**

We strongly support the notion that counterparties can fulfil the clearing obligation in EMIR via Indirect Clearing Arrangements. Smaller market participants completely rely on the possibility to use indirect clearing arrangements. It would be suboptimal indeed if smaller market participants were either not able to conclude derivative contracts which are necessary for their risk management or able to provide certain services only at unattractive prices due to either the lack of intermediaries providing the necessary services or intermediaries providing them at costs which make further provision of services to customers economically non-viable. Small market participants might only account for an insignificant share in derivative markets however their numbers make their access to indirect clearing arrangements an important claim. We ask for equality of their position in comparison to larger market participants. This claim is backed by Recital (33) of EMIR which states the following: “As not all market participants that are subject to the clearing obligation are able to become clearing members of the CCP, they should have the possibility to access CCPs as clients or indirect clients subject to certain conditions.” Unfortunately the content of the recital has neither found access to the legislative text nor the TS so far. Therefore we ask for a realisation of the recital’s claim within the legally relevant part of EMIR (be it in the level 1 text or the Technical Standards).

**Art. 2 ICA para. 2 (Honouring obligations following default)**

The paragraph indicates with regard to indirect clearing arrangements that “clearing member[s have] to honour any obligations between the client and its indirect clients following the default of the client”. We consider this, at least, misleading, as a contractual arrangement between the client and the indirect client cannot be binding upon the clearing member. The agreement between the two parties can therefore only contain provisions setting out an obligation of the client to ensure that the client enters or has entered into a contractual agreement with the relevant clearing member which adequately addresses the consequences of a default of the client on behalf of the indirect client and the relevant transactions.

Furthermore, we would value further clarification on the type of authorisation needed in order to provide indirect clearing arrangements.

**Art. 3 ICA para. 1 (Single aggregated indirect clients’ account)**

We would like to underline that we agree with ESMA’s indirect clearing proposal to provide separate account for client and indirect client’s assets at CCP level. For clarification purposes we would nonetheless suggest some refinements to the article by suggesting to explicitly stating that only a segregate “aggregate indirect client” account and not individual segregated client accounts per indirect client are required at CCP level. ESMA shares this view in the explanatory paragraph 23 lit. b: “for the indirect clients [the CCP] will need to maintain at least one specific segregated account at CCP level.”

**Art. 4 ICA para. 3 (No exposure to losses in case of default)**

The paragraph refers to Article 39 paragraph 9 of the EMIR regulation to define the requirements that need to be met with regard to the obligation to distinguish in accounts with the clearing member the assets held for indirect clients. One of these requirements applying is the obligation to ensure that the positions recorded in an account “are not exposed to losses”. In practice, this will primarily concern collateral posted by the indirect client (specifically, the initial margin) and passed on to the CCP. As this collateral in form of the initial margin will be posted most likely in cash, it is nearly impossible to distinguish this cash transaction from other assets of the party receiving the cash payment. Secondly, even if the initial margin is pledged in securities, variation margins will still require cash which then poses the same problem as above.

As long as there are no harmonised special provisions in the EU requiring national laws to protect client positions in view of the specific circumstances of client clearing against the consequences of an insolvency of the account holder, national insolvency laws will always override any contractual arrangement. It will therefore not be possible to ensure complete protection by contractual means alone.

**Art. 4 ICA para. 7 (Conflict of interest)**

As rightfully stated in the paragraph, the potential conflict of interest between the clearing member and a client offering indirect clearing services should be properly administered. Adequate safeguards should be out in place that information regarding indirect clearing arrangements (including information about the clients of the client offering indirect clearing) remains with the staff of the clearing member responsible for these indirect clearing arrangements.

**Criteria for the determination of the classes of OTC derivative contracts subject to the clearing obligation**

**Art. 1 CRI (Covered Bonds)**

Under Recital 16 of the EMIR regulation, ESMA is asked to take into account the specific nature of OTC derivative contracts which are concluded with covered bond issuers or with cover pools for covered bonds in connection with the determination of the classes of derivative contracts to be subjected to the clearing obligation. Consequently, the regulation appears to grant ESMA the mandate to define criteria under which OTC derivative contracts concluded with covered bond issuers or with cover pools for covered bonds may be classified as not eligible for CCP clearing.

This specific issue is, however, not addressed in the present draft delegated regulation. Does this mean that ESMA intends to address this particular question in another context, i.e. when determining the individual classes of derivative contracts subject to the clearing obligation?

**Public register**

**Art. 1 PR para. 4 (Phase-in)**

The practical implementation of the clearing obligation will be very challenging. Market participants thus need sufficient time to adjust their processes. The clearing obligation therefore needs to be phased in over a sufficient period of time. The draft proposal allows for such a phase-in, however, it appears to limit the possibility to structure such phase-in solely by categories of counterparties. This will almost certainly be too restrictive. The manner in which a phase-in is to occur should be defined on a case by case basis, allowing a significant degree of flexibility, including the flexibility to structure the phase-in on the basis of other categories than counterparties (i.e. sub-categories of products).

**Non-financial counterparties**

**Art. 1 & 2 NFC**

It is important for us to stress that financial market participants cannot be made responsible for controlling whether or not non-financial counterparties have breached the clearing threshold. Article 10 in the EMIR level-1-legislation stresses that NFCs shall be responsible for truthfully and immediately reporting whether they comply with the rules governing the clearing threshold. It should be made clear that financial counterparties can certainly not be obliged to determine by themselves whether or not a non-financial counterparty is actually subject to the clearing obligation

We would welcome further clearer distinction in Article 1 NFC in form of an additional paragraph that clarifies that it is the sole responsibility of the non-financial counterparties (NFC) to monitor their derivatives positions and inform their counterparties accordingly, if they have breached any of the non-clearing thresholds. As only the NFC can be knowledgeable of all of its positions – a view which has been also shared by ESMA during the public hearing on 12 July 2012 in Paris – and in order to create legal certainty of the duties of all counterparties, we would kindly ask for further clarification in the RTS.

As a further step in the interest of legal certainty market participants need to be able to rely on publicly available, official information. The current draft delegated regulation should therefore include provisions requiring the registration of the identity of all non-financial entities subject to the clearing obligation in a public register. Ideally this would be the public register maintained by ESMA. Otherwise, counterparties would be forced to rely solely on the statements of their counterparties on their respective status without any means to verify such statements.

**Risk mitigation for OTC derivative contracts not cleared by a CCP**

**Art. 1 RM paragraph 2 & 3 (Timely confirmation)**

Firstly, we agree with the time limits proposed and the general concept regarding the confirmation of transactions. However, this is based on the understanding that “confirmation” is interpreted in line with current practice as the (first) confirmation of the key terms (term sheet) by one of the counterparties and not any response to such confirmation from the other counterparty. We also assume that it is not expected that such confirmations cover all aspects of the transaction in minute detail but focus on the crucial key data.

Secondly, we believe that the term “electronic means” may need to be defined in more detail. It will be necessary to define what is to be understood under “where available”. Availability should only be assumed where an electronic system can be reasonably expected taking into account the trade volume on the one hand and the cost of implementing and maintaining such system on the other.

Furthermore, to avoid uncertainties we suggest introducing a definition for the terms “business day” and “local time”. In both cases this should be the day and time at the place where the confirming party is situated.

**Art. 2 RM para. 4 lit a. & b. (Portfolio reconciliation)**

Portfolio reconciliation is a very complex endeavour and a daily reconciliation process will be very challenging for smaller financial counterparties. The thresholds regarding the number of outstanding contracts should therefore be reconsidered to take such smaller market participants into account.

We therefore advocate the introduction of additional categories for portfolio reconciliation where at least one category for small (<150 or <100 contracts) portfolios with a quarterly or semi-annual reconciliation frequency and one category for very small (<25 or <10 contracts) portfolios without or with only annual reconciliation.

**Art. 3 RM (Portfolio compression)**

Under the current proposal the counterparties would be required to prepare “a reasonable and valid explanation” to the competent authority in the event the counterparties deem a compression exercise inappropriate.

Portfolio compression can only cover certain of the relevant counterparties’ own positions, never the complete portfolio. For example, positions required for specific hedging purposes need to be maintained. Therefore, the total number of transactions which may be eligible for compression may be significantly lower than the total number of transactions outstanding between two counterparties. The conclusion that a compression exercise is not appropriate may therefore rather become the standard than the exception.

It has to be stated that certain portfolios are not suitable for compression. Compression would only be applicable to own positions and even then not suitable when micro hedging is involved whose effects could be destroyed by replacing individual derivative relations by an overall position.

**Art. 7 RM para. 1 (Intragroup transaction notification details)**

We would like to request further clarification from ESMA with regard to this paragraph, as some of our members express doubt in their interpretation whether intragroup transactions that are exempted under Art. 11 par. 5 of the EMIR Regulation are also excluded in the notification requirement.

**Art. 7 RM para. 2 (Definition of intra-group transactions)**

An intragroup transaction is not only defined by Article 3 para. 1 & 2 of the EMIR Regulation, but is also based on the definition of a “group” which can be found in Art. 2 para. 16. Therefore these two provisions have to be seen as complementary, as Art. 3 is the more specific and detailed provision, but Art. 2 para. 16 provides the groundwork for it. We would consequently assume that where these two provisions differ or are not entirely aligned, the definition of the “same group” in Art. 3 prevails over Art. 2 para. 16 of the Regulation.

**Art. 8 RM lit. d (Intra-group transaction – Information to be publicly disclosed)**

Regarding the public disclosure requirement of an intra-group exemption we are uncertain about the proposed lit. d. The draft asks for “the notional aggregate amount of the OTC derivative contracts for which the intragroup exemption applies” to be published. The Level-1 text of EMIR does not provide a maximum notional exemption for intra-group transactions. We therefore believe that point d should be deleted.

**Ad Annex III: Draft regulatory technical standards on CCP requirements**

**Collateral (COL)**

We do support the trend to only admit very liquid collateral. However we do not understand that there seems to be a tendency to completely exclude equities from being a feasible choice as collateral. There are situations where certain equities are a suitable choice as collateral. However, clearing members and clients as well as client-clients shall not be forced to supply any single one of the two options. They should especially not be forced to supply equities as collateral.

**Ad Annex V: Draft regulatory technical standards on trade repositories**

The new requirements in Annex V set out an obligation to report the market value of the position and the amount of collateral posted in view of every single transaction to be reported. Where we believe that there is some merit in reporting market values, we have doubt that this is possible in all cases. More pressing however seems to be the possibility that from the formulation in the TS-text a constant reporting obligation whenever the market value changes could be derived. We are opposed to a reporting obligation as far reaching as this. We do not believe that EMIR provides for a mandate covering such intensity of reporting.

We support the efforts by ESMA to work towards overlapping EMIR and MiFID requirements in terms of future reporting in order to avoid duplication of reporting. It would be efficient to have one and only one recipient for a certain set of information. However even more pressing than this is the need to minimize the amount of true double reporting where virtually identical information has to be reported to one or more recipients but according to different reporting-tables and using different forms. In short: we find it highly inefficient if counterparties have to report identical content in more than one format to one or more recipients. This may seem a trivial point, but since building up reporting infrastructure has become a main cost driver over the last years and this has the potential of excessively taxing already strained financial institutions, we again stress the importance of not unnecessarily increasing the already heavy reporting burden.

**Interim Identifiers**

The use of ‘interim’ solutions for identifying either contracts or counterparties seems to directly connect to our last point as it would be crucial that ESMA considers carefully the costs of building interim systems which would have to be changed or abandoned after only a very limited time of use. The finalisation of the LEI and UPI standards would be necessary to sensibly set the stage for using a global identification code. We would suggest using current identification methods, possibly extending and amending them in order to make them compliant. It should be a major goal however not to devise a congenial and highly sophisticated (and thus probably difficult and expensive to implement) alternative identifier but to minimize the period of time in which there is no final solution available.

Yours sincerely,

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