

## EFET<sup>1</sup> response to EC public consultation on Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories

■  
13 August 2015

### PART I: Questions on elements of EMIR to be reviewed

#### Question 1.2: Non-Financial Firms

Article 85(1)(b) states that: “ *The Commission shall.....assess, in coordination with ESMA and the relevant sectoral authorities, the systemic importance of the transactions of non-financial firms in OTC derivatives and, in particular, the impact of this Regulation on the use of OTC derivatives by non-financial firms;*”

*Non-financial counterparties are subject to certain requirements of EMIR. However, such counterparties will not be subject to the requirements to centrally clear or to exchange collateral on non-centrally cleared transactions provided that they are not in breach of predefined thresholds, in accordance with Article 10 of EMIR. Further, it is recognised that non-financial counterparties use OTC derivative contracts in order to cover themselves against commercial risks directly linked to their commercial or treasury financing activities. Such contracts are therefore excluded from the calculation of the clearing threshold.*

- (a) i. Are the clearing thresholds for non-hedging transactions (Article 11, Regulation (EU) No 149/2013) and the corresponding definition of contracts objectively measurable as reducing risks directly relating the commercial activity or treasury financing activity (Article 10, Regulation (EU) No 149/2013) adequately defined to capture those non-financial counterparties that should be deemed as systemically important?
  - ii. If your answer to question i. is no, what alternative methodology or thresholds could be considered to ensure that only systemically important non-financial counterparties are captured by higher requirements under EMIR?
- (b) Please explain your views on any elements of EMIR that you believe have created unintended consequences for non-financial counterparties? How could these be addressed?
- (c) Has EMIR impacted the use of, or access to, OTC derivatives by non- financial firms? Please provide evidence or specific examples of observed changes.

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<sup>1</sup> The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent, sustainable and liquid wholesale markets, unhindered by national borders or other undue obstacles. We currently represent more than 100 energy trading companies, active in over 28 European countries. For more information, visit our website at [www.efet.org](http://www.efet.org).

## Response to 1.2 (a), (b) and (c)

In view of the evaluation of these thresholds, the Commission is expected to review the systemic relevance of energy firms this year as provided for by recital 29 of EMIR. Also, the particular characteristics of the energy sector should be taken into account in consultation with the Agency for the Cooperation of Energy Regulators (as also provided for by recital 29).

There is no evidence to support the view that any NFC firm operating in the energy commodity market could be deemed as systemically relevant to the financial system<sup>2</sup>. In addition, a clearing threshold set at €3bn of Gross Notional Value (GNV) of outstanding proprietary OTC commodity derivatives cannot be viewed as representing a ‘systemic’ level beyond which a firm’s activity is relevant to the financial (or even much smaller commodity) market. This level seems rather intended to allow only a limited amount of non-hedging trading activity in OTC commodity derivatives.

It was clear that a comprehensive response to the financial crisis was needed to strengthen financial infrastructures such as central counterparties and EMIR was developed to ensure transparency, reduce credit and operational risk, and improve robustness of market infrastructure in the OTC derivative sector. EMIR has been largely successful in delivering on all of these objectives. It is now appropriate to review whether aspects of the new regulatory framework should be amended in light of market and regulatory developments (both within the EU and in other jurisdictions) to strike an appropriate balance between the regulatory burden faced by firms and improving the stability of OTC derivative markets.

In relation to the EMIR clearing thresholds for commodities a number of points are important in considering whether they remain relevant going forward:

- **A significant amount of OTC commodity derivative activity has now shifted to a cleared environment** – firms (that did not want to be defined as NFC+ entities) responded to the EMIR OTC commodity derivative thresholds in two ways: OTC non-hedging activity was shifted to a cleared environment and/or has been curtailed. This response has meant that the size of the OTC commodity derivative market is now smaller than it was prior to the financial crisis due to the shift of a proportion of standard OTC commodity derivative contracts to central clearing. The majority of the residual activity in OTC markets will be for hedging purposes or will be structured transactions that cannot be centrally cleared.

Commodity derivatives were already a very small proportion of the OTC derivative market<sup>3</sup> and now it is even smaller.

- **The implementation of a new commodity exemption framework under “MiFID II” and related regulatory developments:** It is important that the review of EMIR is not undertaken in isolation from related regulatory developments both in the EU and in other jurisdictions. It is expected under MiFID II that a new licence exemption

<sup>2</sup> “Systemic risk in the energy sector – Is there a need for financial regulation” Marco Kerste, Matthijs Gerritsen, Jarst Weda, Bert Tieben. Energy Policy 78, December 2014.

<sup>3</sup> The proportion of commodity derivatives decreased from 0.5% (H2-2009) to 0.3% (H2-2014) of the global derivatives market. Source: Statistical release OTC derivatives – Bank for International Settlement (www.bis.org).

framework for commodity traders will be introduced from January 2017. While the final framework has yet to be agreed, it is already clear that it will specify limits on the amount of proprietary trading firms can undertake in **all** financial commodity markets – both OTC and cleared markets. In addition, MiFID II will require the setting of position limits on exchange and OTC equivalent commodity derivative contracts, which will provide further additional restrictions on the extent of proprietary trading in financial commodity markets.

Considering these developments, it is appropriate to question whether the continuation of the EMIR OTC clearing threshold *for commodity derivatives* provides additional protection to manage the level of risks. The EC has also committed – in particular through its recently published “Green Paper” – to ensure that the development of legislation (and regulation) is consistent with the objectives to promote employment and growth and that unnecessary or redundant regulation is removed. We believe the EMIR review should be subject to the same scrutiny.

If the EMIR OTC derivative clearing thresholds are continued, firms will effectively be counting the same OTC commodity derivatives activity against three different regulatory restrictions on proprietary trading.

The Commission needs to ensure full consistency between all aspects of the regulatory framework (and in particular between MiFID II and EMIR) in order to avoid any duplication and to alleviate, where appropriate, the complexity of the regulatory framework, consistent with the stated objective of the Commission to promote growth and employment.

The clearing threshold also creates unintended consequences in terms of restricting the ability of those that want to use OTC markets (including end users) from securing efficient and effective options to manage their risks. This is because such activity could be considered as proprietary activity for those providing an OTC derivative hedging service. This factor should also be taken into account in the overall review of EMIR.

If the EC does decide to continue with the thresholds, then a number of changes to the way they operate are needed:

- **Calculation of GNV for the clearing threshold** – GNV is currently calculated on the basis of the open (or residual) gross value of the position. This means that an OTC contract will continue to contribute to the level of GNV until it closes out at expiry. This creates an incentive on NFC- firms to seek to enter into shorter maturity OTC contracts to allow the associated GNV to be ‘recycled’ more quickly. This distortion of behaviour exacerbates the problem of unintended consequences identified above. The result is a potential restriction on the provision of hedging services particularly further along the maturity curve.  
One way of resolving this would be to move to a rolling one year calculation of GNV so that transactions add to GNV only for a one year period regardless of how long they are entered into. This is the approach used in the US under Dodd-Frank for the calculation of GNV against the Swap Dealer thresholds.
- **Netting GNV by counterparty** – the current ESMA Q&A allows firms to net GNV by counterparty for assessment against the EMIR clearing thresholds. This is appropriate as it reflects the underlying (credit) risk position and is consistent with the objectives

of EMIR. It is important that this approach is enshrined in legislation to provide firms with regulatory certainty and as such it should be included in the EMIR Level 2 legislation.

We think, however, that ESMA's understanding of netting is very narrow and unnecessarily restrictive: "Netting per contracts and counterparty should be understood as fully *or partially* offsetting contracts having exactly the same characteristics (type, underlying, maturity, etc.) with the only exception of the direction of the trade and notional amount (in case of partial offset) concluded with the same counterparty."<sup>4</sup> This narrow understanding does not match standard market practice and business rationale with regard to netting by counterparties according to bilateral master agreements in the energy industry. For example, it makes no difference from a (credit) risk management perspective if a 1-year derivative is netted with an opposite 1-year derivative or with opposite 4 quarterly derivative transactions.

The Cascading process for contracts negotiated in the market, beyond month ahead should be recognised:

The Cascading is the process by which in a certain point of time products are fragmented into several products of shorter maturity in such a way that liquidity in the initial contract disappears and the liquidity in the fragmented contracts suffers an increase.

More specifically, cascading is the process through which, on the last trading day after the trading session closing, the existing positions in a e.g. electricity year contract (so called "Calendars") are replaced by new positions in the underlying January, February, March, second quarter (Q2'), third quarter (Q3') and fourth quarter (Q4') at the settlement price of that year. These new positions will be completely fungible with the existing positions in the respective month and quarter contracts.

The same happens with quarters. On the last trading day, the positions are replaced by new positions of identical volume in the three underlying month contracts at the settlement price of that quarter contract's last trading day, which will be completely fungible with the existing positions in the respective month contracts.

The cascading of positions in the year contract is processed at the same time of the cascading of positions of the first quarter contract of the year in question.

The own dynamics and rules of the market are behind this splitting of contracts, and market participants take into account these market rules when deciding the strategies. Cascading process is expressly acknowledged by Spanish and Portuguese Regulators under OMIP rules.

The above-mentioned business practices are valid methods aligned with the level 1 and 2 texts of EMIR which enable to net OTC derivatives contracts that have overlapping periods of validity, meaning that for any such overlapping validity period, the maturity of the contracts is considered the same. We believe it is important to

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<sup>4</sup> "Questions and Answers: Implementation of the Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories (EMIR)" ESMA April 2015, p17.

recognise the validity of such sound practices for calculating positions counting towards the clearing threshold.

- **An appropriate definition of extra-territoriality** – EMIR has a very extensive extra-territoriality reach which also goes beyond the scope of MiFID II, which rightly considers investment activities carried out in the EU. This is not justified in some areas as it creates a significant overlap with the legislation and regulatory framework in other jurisdictions. These overlaps lead to inconsistencies and an unnecessary regulatory compliance burden. This is best illustrated by taking an example of a NFC-group that has a separate legal entity within the overall Group operating in another jurisdiction. For example, if the entity in the non-EU jurisdiction (say in the US) enters into a non-hedging OTC derivative transaction (by providing a hedging service to a *local* power producer or municipality/utility company) it is necessary to count this trade against the calculation of the Group position against the EMIR commodity derivative clearing threshold. In this instance, a transaction which:
  - Is regulated under the general provisions US law
  - Is entered into by two US entities
  - Has no impact on the EU market as it is related to local (and not global) markets
  - Is already subject to the Swap Dealer thresholds under Dodd-Frank,

will count towards the EMIR clearing thresholds. This is not appropriate – and creates additional issues - when the definition of a derivative is different; the definition of what constitutes a hedge is different; and how GNV is calculated is different. Even non-EU exchanges where derivatives are centrally cleared have been considered differently from European regulated markets by ESMA and this adds to the difficulties generated by the extra-territoriality aspects of EMIR.

All jurisdictions have now reformed their financial regulation framework consistent with the objectives of the G20 commitment. Although reforms are not completed everywhere (and are not identical) we are not aware of any significant gaps that justify continuance of the current extra-territoriality reach of EMIR.

Dodd-Frank has established a more appropriate boundary. It does this by requiring firms (regardless of whether they are US established entities) to count against the Swap Dealer thresholds non-hedging OTC derivative transactions that are executed with US established entities. This allows a Group with a trading entity in more than one jurisdiction to take simple steps to ensure an appropriate separation of activity.

A similar approach under EMIR would be appropriate – so that if a non-EU established entity with a corporate Group executes a non-hedging OTC derivative transaction with an EU established entity it would count towards the assessment of the EU established Group against the EMIR clearing threshold.<sup>5</sup>

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<sup>5</sup> One way to implement this approach would be to require that GNV is aggregated across all “non-financial counterparties” in the Group rather than “all non-financial entities” – which is currently the case – although this may require a change to the Level 1 EMIR legislation. Alternatively, an equivalence assessment could be introduced into the Level 2 EMIR legislation such that where another jurisdiction is deemed to have implemented

## Part II: General Questions

### Definitions and Scope

*Title I of the Regulation contains Articles 1-2.*

*Article 1 determines the primary scope of the Regulation, in particular with regard to public and private entities.*

*Article 2 provides definitions in use throughout the Regulation which further determine the scope of application of certain of its provisions.*

### Question 2.1

- i. Are there any provisions or definitions contained within Article 1 and 2 of EMIR that have created unintended consequences in terms of the scope of contracts or entities that are covered by the requirements?
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

### Response to 2.1 (i) and (ii)

#### *Article 2 (7)*

In Article 2(5) the definition of ‘derivative’ or ‘derivative instruments’ should be linked to the definition in MiFID, otherwise that would lead to discrepancies and a non-uniform application of the definition – hence of EMIR – throughout the EU. Market participants need a single regime throughout the EU to limit possible disputes with counterparties and uncertainty when transactions are made in different Member States.

ESMA does not permit firms to exclude from GNV any OTC transactions which are given up for clearing post trade execution (they can only be excluded if given up at the point of execution). Firms should be permitted to realise the GNV benefit of clearing an OTC transaction regardless of when it given up for clearing. This would be entirely consistent with the objectives of EMIR

In article 2(7) it should also be deleted the reference to ‘third country market considered as equivalent to a regulated market in accordance to article 19(6) of [MiFID]. In the text of MiFID II the respective provision does refer only to equity markets and cannot apply in case of EMIR anymore. As recommended above, any derivative that is cleared through a CCP approved under EMIR or for which a decision of equivalence has been taken, should *not* be considered an OTC derivative.

#### *Article 2(16)*

The definition of a Group in Art. 2(16) should be updated with the references to the most recent accounting Directive (Directive 2013/34/EU).

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equivalent reforms to EMIR any transactions executed in that jurisdiction are excluded from the EMIR clearing threshold (unless executed with an EU counterpart).

## Clearing Obligations

*Under EMIR, OTC derivatives transactions that have been declared subject to a clearing obligation must be cleared centrally through a CCP authorised or recognised in the Union. ESMA has proposed a first set of mandatory clearing obligations for interest rate swaps which are yet to come into force. Counterparties are therefore in the process of preparing to meet the clearing obligation, to the extent that their OTC derivatives contracts are in scope of the requirements.*

### Question 2.2

- (a) With respect to access to clearing for counterparties that intend to clear directly or indirectly as clients; are there any unforeseen difficulties that have arisen with respect to establishing client clearing relationships in accordance with EMIR?

If your answer is yes, please provide evidence or specific examples. How could these be addressed?

- (b) Are there any other significant ongoing impediments or unintended consequences with respect to preparing to meet clearing obligations generally in accordance with Article 4 of EMIR?

If your answer is yes, please provide evidence or specific examples. How could these be addressed?

### Article 5

The clearing obligation process may need to be reviewed if the clearing threshold remains to give ESMA more flexibility in the administration of the public register (Art. 6) when removing an asset class from the clearing obligation.

In accordance with ESMA's assessment set out in the CP for CCP clearing of Interest Rates (pages 55-67):

ESMA may need to remove or suspend the clearing obligation on specific classes for a number of reasons including:

- When the composition of market participations dramatically shifts (e.g. fewer clearing members), thereby rapidly impacting the risk profile of the market;
- When there is only one CCP left to clear the contract
- When liquidity dries on a contract e.g. during a financial crisis, because of the migration from rate indices such as LIBOR to potential alternatives, because of the introduction of a new and more attractive substitute to a certain contract;
- When the quality of available market prices deteriorates;
- When the collateral accepted by the CCP is reduced.

Under such circumstances ESMA would need to act as a matter of urgency (within a few days) to remove the clearing obligation from a specific Class+. The procedural delays resulting from the modification of an RTS would not be compatible with this objective.

Any change should be notified by ESMA to market participants with sufficient lead time to allow them to react.

*Article 10.1*

Given the uncertainties in the market around the methodologies for calculation of the notional value of certain contracts, a mandate should be given to ESMA to set basis methodologies for calculation of certain types of contracts, e.g. the options, locational swaps, contracts with volume optionality, contracts with floating/indexed prices, etc. This should be done in consultation with stakeholders and taking into account existing global practices.

*Article 10.3, ESMA Q&A*

If Gross Notional Value is calculated at a group level, companies belonging to the same group should have the option of requesting an exemption from the obligation of calculating its own notional value as long as it is done by the “parent” company or the entity within the group dealing in derivatives. Clarification could be provided to EMIR article 10.3.

There should be a consistent approach in the calculation for the thresholds of EMIR and MiFID II regarding intragroup transactions. The ESMA Q&A provide that two NFC group entities entering into intragroup transactions with each other which does not fall within the hedging definition, should count both sides of the transactions towards the threshold. The total contribution to the group-level threshold calculation would therefore be twice the notional value of the contract, plus the contract with an external counterparty in case this is not risk reducing. This is not consistent with the approach under MiFID II towards the ancillary exemption threshold, which does exclude both hedges as well as intragroup transactions.

Furthermore, intragroup trades should be excluded from the calculation of the notional amount against the clearing threshold as these do not create any additional risk and only reflect back-to-back trades within a group, whereby a trade and the corresponding risk is transferred to ensure the optimization of position and resources.

OTC derivative contracts that are intragroup transactions as described in Article 3 are not subject to the clearing obligation. As recital 38 states, since the submission of those transactions to the clearing obligation may limit the efficiency of those intragroup risk-management processes, an exemption of intragroup transactions from the clearing obligation may be beneficial.

Since the value of the clearing thresholds are set taking into account the systemic relevance of the related risks as stated in Recital 21 of Commission Delegated Regulation (EU) 149/2013, only risks systemically relevant should be considered by the NFC when calculating the notional value of the sum of net positions and exposures.

Moreover, taking into account these intragroup transactions when calculating the threshold may lead to the unfair situation of having to clear future contracts as a consequence of operations which are themselves exempted.

**Issue regarding frontloading obligation:** such obligations create significant pricing and market risk challenges. Even if the classes of derivatives that will be subject to the clearing obligation during the frontloading window will be known by the counterparties, the market participants will be unable to accurately price these trades that will be cleared at a later stage.

## Trade reporting

*Mandatory reporting of all derivative transactions to trade repositories came into effect in February 2014. The Commission services are interested in understanding the experiences of reporting counterparties and trade repositories, as well as national competent authorities, in implementing these requirements. As noted above, ESMA recently conducted its own consultation on amended versions of these standards. This consultation does therefore not seek any views with respect to the content of either Regulation No. 148/2013 and Regulation No. 1247/2012 nor the proposed amended versions.*

### Question 2.3

- i. Are there any significant ongoing impediments or unintended consequences with respect to meeting trade reporting obligations in accordance with Article 9 of EMIR?
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

EFET supports the need for more transparency in derivative markets and improved access to trade information to regulators.

However, the experience with reporting has been largely negative, especially for lack of guidance at detailed level before the starting of the obligations. For instance the fact that ESMA published clarifications on reporting in the form of Q&A the night before the reporting obligation started did not allow for a smooth introduction of the new requirements.

ESMA updated its reporting validation rules at the end of 2014 with a second version due to be implemented as of October 2015. Given the lack of prescription from ESMA on exactly how transaction reporting should be fulfilled, it is likely that there will be a significant number of reporting breaks (i.e. transactions with not all fields matched by counterparties). We believe the problems of reporting breaks are more significant in commodity than in other asset classes, e.g. due to different interpretations of key aspects of the reporting fields on exchange-traded derivatives.

Therefore, we believe that derivative transactions reported between February 2014 and the end of 2015 should not be required to be reconciled. This would ensure that all efforts are concentrated on reporting accurately once all specifications are clear.

We believe that dual reporting should remain, particularly for OTC transactions. A single reporting mechanism could work only for the exchange-traded derivatives (ETDs) due to the following factors:

- Transactions would be reported by the central counterparties/clearing broker and include all the details for NFCs and FCs (so the reporting for ETDs could be the same and uniform).
- Confirmation is done by the central counterparty/clearing broker
- Margining/margin call are done by the central counterparty/clearing broker

The non-reporting counterparty should be allowed to amend the information reported by the CCP or the clearing broker/bank within a reasonable time-frame.

Single-sided reporting for the OTC could create additional complexities:

- Defining the reporting responsibility hierarchy
- Dealing with lifecycle events as a non-reporting entity
- Fulfilling any requirement to ensure accuracy of reports as a non-reporting entity
- Managing reporting interface with all counterparts

Reporting of OTCs should remain dual, i.e. each counterparty reports its leg of the transaction in the same way the counterparty would confirm the transaction.

Small firms - i.e. those that throughout the year trade less than a certain threshold in number of contracts - should be exempted from reporting. In this case the counterparty trading with them will still report its leg. If both firms are below that threshold, they would be exempted. This is to avoid creating an unnecessary burden for small firms.

Intragroup derivative contracts should also be exempted from regular reporting. However those contracts should be made available upon request from ESMA or the relevant national regulatory authority. ESMA and NRAs should be primarily focused on market based transactions – intragroup transactions do not give rise to credit risk issues and reflect the risk mandate against which each entities operates.

### **Risk Mitigation Techniques**

*Risk mitigation techniques are provided for under Articles 11(1) and 11(2) of EMIR and further defined in Commission Delegated Regulation (EU) No 149/2013. Risk mitigation techniques began entering into force in March 2013 and apply to OTC derivative transactions that are not centrally cleared. They include obligations with respect to transaction confirmation, transaction valuation, portfolio reconciliation, portfolio compression and dispute resolution.*

#### **Question 2.4**

- i. Are there any significant ongoing impediments or unintended consequences with respect to meeting risk mitigation obligations in accordance with Articles 11(1) and (2) of EMIR?
- ii. If your answer to (i) is yes, please provide evidence or specific examples. How could these be addressed?

#### *Art. 11.1, ESMA Q&A 5c*

The ESMA Q&A states that the timely confirmation of OTC derivative contracts applies wherever a new derivatives contract is concluded, including as a result of novation and portfolio compression of previously concluded contracts. However, in case of novation, bilateral confirmations are usually not exchanged because the counterparties conclude a novation agreement to which they attach a list of the novated contracts including the main

elements of the concerned transactions. We believe that an exchange of a deal list as an appendix to the novation agreement is sufficient.

*Risk Mitigation Techniques – Compression*

Compression does not bring any benefits to the counterparties. Therefore, it is an unnecessary requirement that although assessed, is only rarely ever completed. We advise to remove the unnecessary requirement to make an assessment of whether compression is beneficial.

*Risk Mitigation Techniques – Timely Confirmation*

ESMA should assess if phasing in the requirement for the mandatory electronic confirmation for all standardised contracts is appropriate. In our view this will support efficient confirmation and reconciliation processes.

*Risk Mitigation Techniques – Reconciliation*

ESMA should review the reconciliation frequency for NFCs and replace the Annual and Quarterly cycles with one single 6-monthly cycle for all entities. An exemption from reconciliation requirement should be available for small NFCs, i.e. NFCs that have less than a certain number of contracts in a 6-month cycle.

*Risk Mitigation Techniques – Intragroup transactions*

The European Commission could evaluate the possibility of adopting a more proportionate approach on risk mitigation obligations, which are complex and onerous for intragroup transactions. More specifically, intragroup transactions are usually undertaken to allocate and manage risk within the corporate Group and as such we believe they should not be subject to risk mitigation requirements.

*Risk Mitigation Techniques – Mark-to-market in portfolio reconciliation*

We think that the present RTS wording is not sufficiently clear in relieving NFCs- from reconciliation of mark-to-market values. This relief is justified by the complexity of this valuation for non-financial entities across all transactions they execute – and it is not appropriate for an NFC- to simply accept the MtM value provided by the counterparty (as the ESMA Q&A suggests), as it may not be consistent with the value calculated for accounting purposes.

### **Exchange of Collateral**

*Article 11(3) of EMIR mandates the bilateral exchange of collateral for OTC derivative contracts that are not centrally cleared. Article 11(15) mandates the ESAs to further define this requirement, including the levels and type of collateral and segregation arrangements required. The ESAs consulted publically on their draft proposals in the summer of 2014.*

*The ESAs are now in the process of finalising these draft Regulatory Technical Standards. It is therefore recognised that the final requirements are not fully certain at this stage. The Commission services are not seeking comment on the content on the proposed rules published by the ESAs. Nonetheless the Commission services welcome any views from stakeholders on implementation issues experienced to date.*

#### **Question 2.5**

- i. Are there any significant ongoing impediments or unintended consequences anticipated with respect to meeting obligations to exchange collateral in accordance with Article 11(3) under EMIR?
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

It is necessary for NFCs to continue using commercial bank guarantees as collateral. The use of bank guarantees by energy companies does not increase market risk since energy companies own capital investments in assets such as production plants and commodities which could be liquidated in case of failure to pay. Moreover, no bank will issue a bank guarantee without any 'capital substance' behind a NFC.

The ban on using commercial bank guarantees will entail a significant increase of NFCs costs and consequently, a large withdrawal from the market. This will bring less liquidity and transparency. As a result, competition and efficiency will be reduced - what will ultimately lead to higher energy bills for consumers.

### **Cross-Border Activity in the OTC derivatives markets**

*OTC derivatives markets are global in nature, with many transactions involving Union counterparties undertaken on a cross-border basis or using third country infrastructures. EMIR provides a framework to enable cross-border activity to continue whilst ensuring, on the one hand, that the objectives of EMIR are safeguarded and on the other hand that duplicative and conflicting requirements are minimised.*

#### **Question 2.6**

- (a) With respect to activities involving counterparties established in third country jurisdictions; are there any provisions or definitions within EMIR that pose challenges for EU entities when transacting on a cross-border basis?

If your answer to (i) is yes, please provide evidence or specific examples. How could these be addressed?

- (b) Are there any provisions within EMIR that create a disadvantage for EU counterparties over non-EU entities?

If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

As we outlined above, non-EU entities that are part of an EU group should not be subject to the clearing thresholds applied to the EU group, i.e. its derivative activity should not count against the EMIR threshold of the EU group to which it belongs. With such a level of extraterritoriality a US entity part of an EU group is subject to both EMIR and Dodd Frank thresholds. There is a great disadvantage in this respect for firms part of an EU group that are established in third countries.

Article 10.3 of EMIR should require the GNV aggregation by all “Non-Financial Counterparties” in the Group and not including “all non-financial entities”. In addition, if the non-EU entity trades with an EU entity, this should count in the GNV of the group if not a hedge – to avoid incentives to trade in the Europe via a non-EU entity.

### **Transparency**

#### **Question 2.7**

*The overarching objective of the trade reporting requirement under EMIR is to ensure that national competent authorities and other regulatory bodies have data available to fulfil their regulatory mandates by monitoring activity in the derivatives markets.*

- i. Have any significant ongoing impediments arisen to ensuring that national competent authorities, international regulators and the public have the envisaged access to data reported to trade repositories?
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

An important requirement that TRs should be subject to is transparency. TRs should publish aggregated data (volume and value traded) per commodity so that firms could assess themselves against the MiFID II thresholds. It is important that this is done as a matter of priority before any EMIR legislative changes, as the MiFID exemption regime is expected to become operational from January 2016.

### **Requirements for CCPs**

*Titles IV and V of EMIR set out detailed and uniform prudential and business conduct requirements for all CCPs operating in the Union. CCPs operating prior to EMIR's entry into force are required to obtain authorisation in accordance with the new requirements of EMIR, through the EU supervisory college process.*

#### **Question 2.8**

- (a) Are there any significant ongoing impediments or unintended consequences with respect to CCPs' ability to meet requirements in accordance with Titles IV and V of EMIR?

If your answer is yes, please provide evidence or specific examples. How could these be addressed?

- (b) Are the requirements of Titles IV and V sufficiently robust to ensure appropriate levels of risk management and client asset protection with respect to EU CCPs and their participants?

If your answer is no, for what reasons? How could they be improved?

- (c) Are there any requirements for CCPs which would benefit from further precision in order to achieve a more consistent application by authorities across the Union?

If your answer is yes, which requirements and how could they be better defined?

The use of bank guarantees as collateral for CCPs is an important topic that needs to be considered further. In Title IV, Art. 46 of EMIR allows the use of bank guarantees as collateral by non-financial clearing members. Secondary legislation needs to clarify under which circumstances bank guarantees can be used (Art. 46 Para. 2 of EMIR). The related Regulation No 153/2013 requires full backing of these bank guarantees after a grace period of three years, recognising the negative effects of a backing requirement for commodity markets. However, the requirement in the EMIR Implementation Act for full backing after this period in practice negates the use of bank guarantees. Such a requirement is not in line with the EMIR Level 1 text, which does not require non-financial clearing members to post further collateral in addition to a bank guarantee. The three year grace period allowed for power and gas in Article 62 of the EMIR Implementation Act does not remedy the deficiency, considering that this period will be over in less than a year's time. We propose to allow bank guarantees without full backing, by not maintaining section 2.1, point h) in Annex 1 in Regulation No 153/2013.

Until a decision on the use of bank guarantees is made, we kindly request to extend the transitional period of three years.

### **Requirements for Trade Repositories**

*Titles VI and VII of EMIR set out detailed and uniform requirements for all trade repositories operating in the Union. Trade repositories operating prior to EMIR's entry into force are required to obtain authorisation by ESMA in accordance with the requirements of EMIR. To date, ESMA has authorised six trade repositories. ESMA is the primary supervisor for Union trade repositories and has the power to issue fines for non-compliance with the requirements of EMIR.*

#### **Question 2.9**

- i. Are there any significant ongoing impediments or unintended consequences with respect to requirements for trade repositories that have arisen during implementation of Titles VI and VII of EMIR, including Annex II?
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

For the transaction reporting regime to work effectively, TRs should ensure that there is effective interoperability between all TRs. TR validation rules must be rigorously enforced, so that the quality and consistency of transaction reports are high.

Regulators need to provide sufficient clarity on exactly what has to be reported in each field – using example transaction reports (as ACER is doing for REMIT) will help. Some fundamentally different approaches remain (e.g. reporting of ETDs), which undermines the possibility of matching transactions. The solution would be applying the single-sided reporting requirement of ETDs. If regulators do not provide sufficient clarity, then TRs should implement translation tables for 'operational' differences (e.g. date conventions).

There should be a requirement to rectify breaches in a specified time period (longer than 48hrs if double-sided reporting is retained).

### **Additional Stakeholder Feedback**

*In addition to the questions set out above, the Commission services welcome feedback from stakeholders on any additional issues or unintended consequences that have arisen during the implementation of EMIR which are not covered by those questions.*

#### **Question 2.10**

- i. Are there any significant ongoing impediments or unintended consequences with respect to any requirements or provisions under EMIR and
- ii. If your answer to i. is yes, please provide evidence or specific examples. How could these be addressed?

As a general observation, we note that collateral requirements are leading smaller non-financial counterparties to cease direct participation in the market in order to avoid margining costs and to use market access through others. This increases market concentration and reduces liquidity, which ultimately results in higher costs for hedging. These are clearly unintended consequences which are contrary to the objectives of EMIR.

While for many key implementation issues ESMA have gone through RTS/ITS and related adoption processes, including public consultations, a number of very important implementation topics have been dealt with by means of Q&As. Q&As have not been subject to consultation processes, although they may have a material impact on market participants' interpretation, implementation projects and EMIR compliance. A formal process should be put in place around the publication, consultation and entry into force of Q&As.