

ESMA
103 rue de Grenelle
75007 Paris

13 February 2015

LCH.Clearnet Group Limited response to ESMA consultation paper on the review of the technical standards on reporting under Article 9 of EMIR

Dear Sirs,

LCH.Clearnet Group Limited ("LCH.Clearnet")¹ appreciates the opportunity to comment on the ESMA consultation paper on the review of the technical standards on reporting under Article 9 of EMIR.

LCH.Clearnet is a leading multi-asset class and multi-national clearing house, serving major international exchanges and platforms as well as a range of OTC markets. It clears a broad range of asset classes, including: securities, exchange-traded derivatives, commodities, energy, freight, foreign exchange derivatives, interest rate swaps, credit default swaps and euro, sterling and US dollar denominated bonds and repos. LCH.Clearnet works closely with market participants and exchanges to continually identify and develop innovative clearing services for new asset classes. LCH.Clearnet is majority owned by the London Stock Exchange Group ("LSEG"), a diversified international exchange group that sits at the heart of the world's financial community.

LCH.Clearnet appreciates the opportunity to comment on the consultation paper and supports ESMA's objective to address some of the issues encountered with the implementation of the reporting requirements under EMIR. A revised set of rules, which take into account the clarifications made in the ESMA's Q&A and the industry feedback to this consultation, should ensure a more consistent and harmonised approach to reporting.

Overall comments

- Generally, LCH.Clearnet supports the proposals made by ESMA and, where it feels necessary, suggests alternative approaches to ensure that new requirements are implemented effectively taking into account of differences in terms of reporting systems, type of reporting counterparties and type of products.

¹ LCH.Clearnet Group Limited consists of three operating entities: LCH.Clearnet Limited, the UK entity, LCH.Clearnet SA, the Continental European entity, and LCH.Clearnet LLC, the US entity. Link to the Legal and Regulatory Structure of the Group:
http://www.lchclearnet.com/about_us/corporate_governance/legal_and_regulatory_structure.asp

- We note that some of the proposed changes will require significant development and testing efforts. We would therefore like to stress the importance of allowing sufficient lead time for the changes to be implemented smoothly by the authorised Trade Repositories (TRs) and the reporting counterparties.
- Given the scale and breadth of the proposed changes, we believe that the reporting counterparties, including CCPs, would need a minimum of 12 months to plan and implement these changes. ESMA should recognise that this timeline is dependent on the publication of updated report specifications by TRs and not the publication of the revised ESMA's Technical Standards.

Responses to questions

Q1. Do you envisage any difficulties with removing the 'other' category from derivative class and type descriptions in Articles 4(3)(a) and 4(3)(b) of ITS 1247/2012? If so, what additional derivative class(es) and type(s) would need to be included? Please elaborate.

The products currently centrally cleared by LCH.Clearnet are standardised enough to fall within the specific derivative class and type descriptions contained within these Articles so removal of the 'Other' category would not cause any difficulties.

However, LCH.Clearnet recognises that removing this category could create issues for other counterparties trading more complex/structured products or, should LCH.Clearnet's service evolve to support the clearing of more complex/structured products, it is envisaged that initially there may be a use for this 'Other' category. Longer term, more accurate reporting of these types of products may require the introduction of new categories but maintaining the 'Other' category would enable the immediate reporting of these transactions to trade repositories (TR) without the additional development and testing effort required to support a change of this type.

LCH.Clearnet appreciates that the removal of this category is likely to be driven by the volume of reports being submitted with this category which, in itself, provides little value in helping achieve the objective of identifying the derivative asset class and type so understands the reasons behind ESMA's proposal to remove it. However, as a matching field, removal of this category will force reporting counterparties, currently using it, to arbitrarily select the next 'most suitable' alternative. Population of a category that is not 'Other' may lead to a misconception that the correct derivative class and type is now being selected but, in practice, it is likely to lead to a reduction in the quality of the reports as the mismatch rate increases.

A suggested short term alternative solution to the removal of this category could be for ESMA to solicit feedback on the use of this category to understand why it is being used and, based on this feedback, provide further guidance on the use of the remaining categories, unless it necessitates the requirement to add additional categories.

Q2. Do you think the clarifications introduced in this section adequately reflect the derivatives market and will help improve the data quality of reports? Will the proposed changes cause significant new difficulties? Please elaborate.

LCH. Clearnet is supportive of the clarifications introduced in this section and, apart from the clarifications provided in Paragraph (25) on the Buy/Sell indicator, believe that they will have a positive impact on the quality of the data contained in the reports and cannot foresee any difficulties with their implementation.

LCH.Clearnet recognises that clarification of the buy/sell indicator in Paragraph (25) was required as current practice is not standardised across asset classes so, a lack of clarification at this level, is likely to result in matching issues. Although Article 3(a) provides clarification by asset class, which is useful, we believe that in certain circumstances the logic would be complex to implement and is not comprehensive enough to cover all scenarios. For example, further clarification from ESMA would be required to understand what the Buy/Sell indicator should be populated with for a Float / Float i.e. basis swap, where there is no fixed rate paid, and FRAs where the terminology used is different and so does not seamlessly translate into a 'buyer' or a 'seller'.

LCH.Clearnet would recommend ESMA consider an alternative approaches for those products that are not 'bought' or 'sold' e.g. Interest Rate Swaps. The simplest approach would be for the relevant asset class specific fields to be augmented to include whether leg 1 is being paid or received by the reporting counterparty. Alternatively, the existing fields could be maintained with the Trade Repositories (TRs) performing an additional validation of the buy / sell field to match each specific leg and validate that both reporting counterparties agree that one side is paying and the other is receiving the same leg. LCH.Clearnet does not consider this to be complex logic for TRs to implement.

In the case of Foreign Currency Swaps or Forwards, the reporting of the Buy/Sell indicator, as defined in Article 3(a), may work in principle for Non Deliverable Forwards (NDFs) as only USD is exchanged but proves complex and ambiguous for other FX products as it requires that end users of the reported data have prior knowledge and understanding of the business logic being proposed in this Article. To avoid this, ESMA may wish to introduce additional fields such that the data explicitly indicates which currency is being bought or sold. Alternatively, ESMA could follow one of the approaches outlined above.

Q3. What difficulties do you anticipate with the approaches for the population of the mark to market valuation described in paragraphs 21 or 19 respectively? Please elaborate and specify for each type of contract what would be the most practical and industry consistent way to populate this field in line with either of the approaches set out in paragraphs 21 and 23.

If ESMA is trying to capture the exposure inherent to the unrealised PnL of a derivative contract, LCH.Clearnet supports the proposal described in paragraph 23 of using the replacement cost for all derivatives. LCH.Clearnet would like ESMA to confirm whether our assumption is correct and clarify that products for which PnL is:

- realised/settled on a daily basis would have a replacement cost of 0 apart from options whose premiums are paid upfront, where the replacement cost would equal the premium on the replacement trade.
- not realised/settled on a daily basis would have a replacement cost that equals to the Net Present Value apart from options whose premiums are paid upfront, where the replacement cost would equal the sum of the Net Present Value and the premium on the replacement trade.

On this basis, LCH.Clearnet would support the approach set out in Paragraph 23 in favour of that in Paragraph 21.

Q4. Do you think the adaptations illustrated in this section adequately reflect the derivatives market and will help improve the data quality of reports? Will the proposed changes cause significant new difficulties? Please elaborate.

The adaptation provided within Paragraph 29 will not impact the quality of the reports generated by LCH.Clearnet as LEIs are currently used as the identifier for the counterparties to the cleared transaction. However, LCH.Clearnet acknowledges that removing the possibility to enter less robust codes such as Interim Entity Identifier, BIC or Client Codes for counterparties eligible for a LEI could be an issue for smaller market participants and therefore the removal of these codes is unlikely to improve the data quality of the reports.

LCH.Clearnet supports the removal of the flag indicating whether the other counterparty is within the EEA or not as this requires each reporting party to maintain static data required for determining EEA eligibility. Populating the proposed new field, 'Country of the other Counterparty', shifts eligibility determination away from the reporting party to central management by the TRs.

Although LCH.Clearnet supports the renaming of the Transaction Reference Number field, to avoid confusion with the Transaction Reference Number within MiFID transaction reporting, it is in agreement with the EACH proposal to rename this field to 'Unique execution number' rather than the proposed 'Report tracking number'. This is because the aim of this reference is to identify packages of trades related to the same execution and we believe that the term 'Report tracking number' implies uniqueness to a report, rather than a number of reports that relate to the same execution.

LCH.Clearnet would also request clarification from ESMA that they are not expecting the proposed 'Report tracking number' to be populated for position reports; it is only relevant to trade reports.

LCH.Clearnet welcomes clarification on the definition of the format for time periods but believes that a more prescriptive logic is required as the proposed definitions can be interpreted in multiple ways, all of which are correct. For example, every year can be specified as '365D', '52W' or '1Y'.

In principal, LCH.Clearnet supports the proposal that reports containing incorrect data should be corrected using a new action type code 'R'(correction) instead of the current approach of cancelling them using the action code 'E' and then resubmitting a new report using the action type code 'N', as we recognise that doing so would reduce the number of reports. However, ESMA should acknowledge that in practice different systems process transaction updates in different ways so it may not be possible for all systems to differentiate between a record that needs to be reported with an action type code of 'R', as it is a correction, rather than a 'N', as it is a new report.

Take for example a transaction that was originally booked with an erroneous notional amount on a system that does not support updates to a trade. As it is not possible to amend the notional on the original trade (that had already been reported with an action type code of 'N') a new correction trade would be booked to account for the erroneous notional amount. Given that there is no audit trail/systematic linkage between this new correction trade and the original trade, i.e. the new correction trade is not an updated version of the original trade, then there is no means for that system to identify that the new correction trade should be reported with an action type code of 'R' (as it is a correction of the original trade) rather than 'N'.

It has already been proved that all systems can handle the current approach for reporting corrections, namely submitting a cancellation report as an 'E' and then resubmitting a new report with a 'N'. LCH.Clearnet would suggest that systems that can only process modifications as a cancellation and a new could not support the approach being proposed in Paragraph 41.



With the removal of the 'O' action type code, LCH.Clearnet would ask ESMA to provide clarification on which action type code ETD 'give up' and 'take up' transactions should be reported under. The current approach is to report an action code of 'N' and, upon 'take up' or 'give up' by the same or another Clearing Member, submit a new report with an action code of 'O'.

We would like ESMA to confirm that the approach detailed in Paragraph 42 would render the action type 'N' redundant for ETDs, as these are compressed into positions at the end of the day, and is therefore only relevant for OTCs. Notwithstanding the fact that the proposed approach will eliminate the majority of duplicate reports that currently account for compression of a transaction into a position, it is important for ESMA to acknowledge that compression of OTC transactions will still continue to be reported with an action type of 'N' followed by an update with an action type of 'Z' as compression for an OTC, unlike an ETD, is not a lifecycle event that is certain to occur.

Q5. Do you think the introduction of new values and fields adequately reflect the derivatives market and will help improve the data quality of reports? Will the proposed changes cause significant new difficulties? Please elaborate.

LCH.Clearnet welcomes the proposals introduced in Paragraphs 43 and 44 that enable the distinction between reports at the trade and position level and the population of negative values, where appropriate, (respectively).

For reasons similar to those provided in the commentary to Question 7 on Paragraph 30, LCH.Clearnet suggests that, rather than making the reporting counterparty responsible for providing the static data associated with a counterparty to the report (in this case, the country code of the main residence of the other counterparty), all counterparty static should be centrally sourced and maintained as part of the LEI reference data. Paragraph 29 provides evidence of ESMA's support for the use of LEI above other less robust identifiers. Only where the reporting counterparty is not able to populate the report with the LEI of the other counterparty, should the static in the new field 'Country of the other Counterparty' be required to be populated, and subsequently created and maintained, by the reporting counterparty.

LCH.Clearnet supports the proposals contained in Paragraph 47 and 48 to split instrument identification and classification into two separate data fields. The reason for such support is based on the condition that these fields are not mandatory to populate as there is no endorsed UPI in Europe at present and CFI is not used for identification of OTC products.

To support the effective reporting of Credit Default Swaps (CDS) single names on corporate entities, LCH.Clearnet believes the Underlying field should enable reporting parties to clearly identify the entity on which the transaction provides protection. The proposed permitted values, currently listed in Underlying identification type (Table 2, Field 7), do not always allow for this to be the case. For example:

- LEI - Entities referenced under a CDS transactions do not necessarily have a Legal Entity Identifier
- ISIN - Reporting an ISIN as the underlying for CDS single name is not necessarily accurate or even possible because:
 - CDS protection can be on the issuer or on the guarantor of the bond used as Reference Obligation. In this case using the ISIN is ambiguous.
 - A single name CDS can be executed without a Reference Obligation, in which case the "dummy ISIN" "XSNOREFOBL00" is used. In this case the ISIN provides no information about the underlying single name.

LCH.Clearnet feels it would be prudent for ESMA to consider the changes introduced by the industry in 2014 with the implementation of Standard Reference Obligations. The market practice is to confirm such transactions using "dummy ISIN" values such as "XSSNRREFOBL0" to indicate that the applicable reference obligation ISIN for the relevant entity is the ISIN found on the Standard Reference Obligation List published by ISDA.

As a consequence, LCH.Clearnet recommends that a new mandatory field should be added within the new dedicated section (2.i) on Credit Derivatives to report the full legal entity name of the Reference Entity for that CDS (as detailed again in the answer to Question 9.). This will guarantee that the underlying can be identified. Furthermore, LCH.Clearnet recommends that populating the Underlying field with an LEI or ISIN for a corporate single name CDS should be optional.

For a sovereign single name CDS, LCH.Clearnet agrees with the proposal to report the relevant ISO 3166 country code as this should allow for the clear identification of the Reference Entity.

LCH.Clearnet supports the idea of providing the regulators with more information on collateralisation as this is a key element to assess systemic risk in the derivatives market. Although this would represent significant development effort, LCH.Clearnet supports the new requirement to report received collateral and the split between Initial Margin (IM) and Variation Margin (VM).

However, LCH.Clearnet would like to stress that significant clarifications should be made regarding collateral reporting. In doing so, the following points should be considered:

- Collateral received from our Clearing Members is a net payment. No differentiation is made between the collateral that has been received to meet the IM requirement and the collateral that has been received to meet the VM requirement.
- The collateral received from Clearing Members is comprised of more than just their IM and VM requirements, e.g. excess margin is likely to be posted in addition to just the IM requirement and cashflows (coupons, option premiums, etc), price alignment interest, clearing fees, interest etc, are likely to form part of the VM requirement posted. Hence the aggregated value of the IM and VM requirement is unlikely to equal the exposure and margin requirement calculated by the CCP.
- We question at which level should the collateral be reported: whether for each of our Clearing Members the collateral be reported at an aggregate Member and Client level or it should be reported separately as they are separate portfolios. If they are to be reported separately, then to what level this should be taken on the client side: whether it should be taken down to each Individually Segregated Account and Omnibus Segregated Account. Clarification on these points are needed because the level of granularity required will depend on whether there is a requirement to link collateral to each specific client portfolio.

As explained above, LCH.Clearnet believes that by providing constructive information on the collateralisation of market participants, it is fundamental to understand the distinction between IM and VM requirements and collateral received. We would therefore propose to use three fields for collateral:

- Collateral posted/received - ESMA to acknowledge that this will equate to total collateral posted, so will be inclusive of components as excess margin, cashflows, interest, etc
- IM requirement - ESMA to clarify what the component of the IM requirement should be, i.e. should it include IM adds ons/multipliers?
- VM requirement

LCH.Clearnet welcomes the idea of clearly defining responsibilities for UTI generation. However, we believe that the current proposal is ambiguous as it states that for centrally executed and cleared trades the entity responsible for generating the UTI can be **either** the CCP or the execution venue.

(a) for centrally executed and cleared trades the unique trade identifier shall be generated either by the execution venue for its member or at the point of clearing by the CCP for the clearing member. Subsequently, the unique trade identifier should be generated by the clearing member for its counterparty;

In line with the amendment to Article 2(1) where, *'In the case where a contract is concluded on a trading venue and cleared on the day of execution, it is sufficient to report the trade in its cleared form'*, and to eliminate any uncertainty with respect to the generating party for all centrally-cleared trades, LCH.Clearnet propose the following:

(a) for centrally executed and cleared trades the unique trade identifier shall be generated at the point of clearing by the CCP for the clearing member. Subsequently, the unique trade identifier should be generated by the clearing member for its counterparty;

LCH.Clearnet also has concerns around the practical application of 2 (d) (iii) in Article 4a:



(iii) within the same group of entities the seller generates the unique trade identifier.

For the same reasons as detailed in the response to Question 2, the terminology 'buyer' and 'seller' does not seamlessly translate for certain product types, e.g. FRAs.

Q6. In your view, which of the reportable fields should permit for negative values as per paragraph 40? Please explain.

LCH.Clearnet supports negative values for the following reportable fields:

- Value of contract (Table 1, Field 17)
- Price / rate (Table 2, Field 16)
- Notional (Table 2, Field 19 (Original notional) and Field 20 (Actual notional)). Additional feedback on these two new fields has been provided in Question 11
- Up Front Payment (Table 2, Field 23)
- Quantity (Table 2, Field 22)

Whilst LCH.Clearnet recognises the value in ESMA specifying whether a field can be negative and in which circumstances they expect negative values to be reported, (e.g. a negative value in the Up Front Payment field would indicate that a payment was made by the reporting counterparty), we think that being too prescriptive in the specification of the number of numerical characters is very likely to create erroneous data quality issues. For example, the Up Front Payment field is limited to 10 numerical characters and Original notional and Actual notional limited to 20 numerical characters. For currencies such as JPY or HUF this may not be a sufficient number of numerical characters

Q7. Do you anticipate any difficulties with populating the corporate sector of the reporting counterparty field for non-financials as described in paragraph 42? Please elaborate.

As a CCP, LCH.Clearnet does not fall within the definition of a non-financial counterparty (NFC), so the introduction of this additional static does not impact us directly. However, LCH.Clearnet acknowledges that this could represent a significant impact for any Clearing Members, CCPs or third party service providers whom NFCs have delegated their reporting obligation to.

Paragraph 30 states that 'ESMA does not expect this information to be included in the LEI reference data'. LCH.Clearnet suggests that were this information available within the LEI reference data then delegated reporting parties would not need to independently create and maintain this static and consistency of the data, irrespective of the party to whom reporting has been delegated, could be assured. Only where a LEI is not available for the reporting counterparty, should the static in this field be required to be populated, and subsequently created and maintained, by the reporting counterparty.

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

LCH.Clearnet request that ESMA provide clarification that the approach described for the identification of indices and baskets applies only to OTC products, as we concur with the feedback provided by EACH that exchange traded derivatives are standardised and the constituents of any indices or baskets is publicly available information. Replicating this information with every reported record would therefore be superfluous and potentially result in inconsistencies in the quality of the data provided.

For the reporting of indices referenced in CDS Index transactions, as ISINs are not available, LCH.Clearnet supports the proposal to report the full name of the index assigned by the index provider.

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

LCH.Clearnet supports the introduction of this dedicated section to enable the reporting of these standard CDS specific details but believes the following clarifications would improve the quality of the data reported:

- Coupon – although it is specified that the coupon is to be expressed as a percentage, this requires further clarification. For example, should a 5% coupon be expressed as 5.0 or 0.05? LCH.Clearnet also suggests that the field is renamed to 'Fixed Rate'. This is in line with market convention and 'Coupon' may be considered slightly ambiguous as it could relate to either a rate or an amount and only reference to the field description qualifies it to be the former.
- Date of last lifecycle event – confirmation of the full list of lifecycle events is required. For example, is a coupon event considered a lifecycle event?

As detailed in the response to Question 5, LCH.Clearnet suggests that an additional field is added to this section to contain the full legal entity name of the Reference Entity to enable the identification of the underlier for the reporting of single name CDS products.

Q10. The current approach to reporting means that strategies such as straddles cannot usually be reported on a single report but instead have to be decomposed and reported as multiple derivative contracts. This is believed to cause difficulties reconciling the reports with firms' internal systems and also difficulties in reporting valuations where the market price may reflect the strategy rather than the individual components. Would it be valuable to allow for strategies to be reported directly as single reports? If so, how should this be achieved? For example, would additional values in the Option Type field (Current Table 2 Field 55) achieve this or would other changes also be needed? What sorts of strategies could and should be identified in this sort of way?

LCH.Clearnet believes that the reporting of strategies as a single report conflicts with the way they are represented within our systems and also with the way in which they are priced and valued. Any benefit resulting from this suggested approach would be outweighed by the complexities involved with implementation.

Rather than synthetically creating a single report, LCH.Clearnet would support the adoption of a flag enabling identification of multiple reports relating to a single strategy. However, as a CCP, the population of this flag would be dependent on this information being available at the time that the transactions making up the strategy were cleared and would not be something that could be determined by the CCP themselves.

Q11. Do you think that clarifying notional in the following way would add clarity and would be sufficient to report the main types of derivatives:

- 60. In the case of swaps, futures and forwards traded in monetary units, original notional shall be defined as the reference amount from which contractual payments are determined in derivatives markets;**
- 61. In the case of options, contracts for difference and commodity derivatives designated in units such as barrels or tons, original notional shall be defined as the resulting amount of the derivative's underlying assets at the applicable price at the date of conclusion of the contract;**
- 62. In the case of contracts where the notional is calculated using the price of the underlying asset and the price will only be available at the time of settlement, the original notional shall be defined by using the end of day settlement price of the underlying asset at the date of conclusion of the contract;**
- 63. In the case of contracts where the notional, due to the characteristics of the contract, varies over time, the original notional shall be the one valid on the date of conclusion of the contract.**

LCH.Clearnet would like to stress that the concepts of:

- original notional cannot be applied to exchange traded derivatives as these transactions are reported only once at the end of the day that they were traded and then compressed into positions.
- actual notional cannot be applied to FX OTC products

For some OTC transactions, where a distinction between original and actual notional is applicable, e.g. Variable Notional Swaps, it would be necessary to create a new lifecycle event to trigger reporting of the updated actual notional as, in practice, such an event is contract intrinsic and not a lifecycle event as such. Given the emphasis of this change is to improve the quality of reporting, LCH.Clearnet would propose that instead of creating a distinction between original and actual notional as well as creating an artificially imposed lifecycle event that would enable reporting of the updated actual notional value, the full notional schedule (according to ISDA standards) is reported with the original report. Although this recommendation would seem to imply repeating fields or repeating attributes within a field, LCH.Clearnet would be open to working with ESMA and/or industry groups to define the best approach to incorporate this repeating data into the existing format.

LCH.Clearnet would also require further clarification on how a distinction between original and actual notional values would be populated for credit index trades. Contractual payments for credit index trades include the index factor in their calculation:

Coupon = notional * index factor * fixed rate

The trading and confirmation convention is to state the notional without taking into account the Index Factor, even if the index factor <1.00 when the trade is executed. The index factor can also change over the life of the trade due to credit events, whilst the trade notional itself is not modified.

We would like to clarify if the actual notional should reflect the index factor. If so, for a trade executed when the index factor is <1.00 the actual notional will be different from the original notional from the outset. In this context, LCH.Clearnet proposes that having a trade notional and an effective notional (on which the protection is calculated) would be more sensible.



We hope that this response will assist ESMA in the development of revised reporting requirements under EMIR. Please do not hesitate to contact myself or my colleague Jonathan Kemp, Executive Director of Group Operations, at Jonathan.Kemp@lchclearnet.com should you need any clarification on this response or wish to discuss further.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'MR', with a large, sweeping flourish extending to the right and a small 'c' at the end.

Martin Ryan
Group Head of Technology and Operations