



European Securities and
Markets Authority

Reply form for the consultation paper on indirect clearing arrangements under EMIR and MiFIR



5 November 2015

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the questions listed in this Consultation Paper on Indirect clearing arrangements under EMIR and MiFIR, published on the ESMA website.

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
- do not remove the tags of type <ESMA_QUESTION_RTS_INDIRECT_CLEARING_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
- if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that ESMA should consider

Naming protocol

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA_RTS_INDIRECT_CLEARING_NAMEOFCOMPANY_NAMEOFDOCUMENT.

E.g. if the respondent were XXXX, the name of the reply form would be:

ESMA_RTS_INDIRECT_CLEARING_XXXX_REPLYFORM or

ESMA_RTS_INDIRECT_CLEARING_XXXX_ANNEX1

To help you navigate this document more easily, bookmarks are available in “Navigation Pane” for Word 2010 and in “Document Map” for Word 2007.

Deadline

Responses must reach ESMA by **17 December 2015**.



All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input/Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading [Legal Notice](#).

Introduction

Please make your introductory comments below, if any:

<ESMA_COMMENT_RTS_INDIRECT_CLEARING_1>

[This is the response of the London Stock Exchange Group (LSEG), a financial market infrastructure provider, headquartered in London, with significant operations in Europe and North America. LSEG welcomes the opportunity to respond to ESMA's Consultation Paper on indirect clearing under EMIR for OTC derivatives and under MiFIR for ETDs.

This response reflects the views of the EMIR authorised CCPs operated by LSEG, namely LCH.Clearnet Ltd, LCH.Clearnet SA and Cassa di Compensazione e Garanzia (CC&G).

We support the ESMA's proposals which aim to align the requirements on indirect clearing under EMIR for OTC derivatives and under MiFIR for ETDs in order to avoid potential conflicting rules; and enhance the resilience of indirect clearing arrangements in light of the concerns highlighted by the industry on the degree of protection of indirect clients' positions.

LSEG's response focuses on the relevant questions and makes the following points:

- It notes some concerns on the asset segregation in the newly proposed account structures, which we believe may not necessarily provide an equivalent level of protection to that referred to in Article 39 and 48 of EMIR (the probability of porting is low and there are difficulties in the allocation of excess collateral to indirect clients). Moreover, the gross omnibus account structure will heavily rely on the quality of the information to be passed across the clearing chain, and as a result it will not ensure straight-through-processing, potentially giving rise to increased operational costs.
- It encourages ESMA to clarify that it is not the intention of the new rules to expect CCPs to manage the positions of indirect clients and perform the leapfrog payments in respect to any indirect clients at any point in the chain.
- It suggests amendments to the RTS text to ensure that the CCP will not be required to allocate any excess collateral it receives from the clearing member for the account of indirect clients to each indirect client, as it would be costly and complex.
- It supports the requirement whereby, if the proposed gross omnibus accounts will be implemented, the clearing member will need to provide to the CCP all the necessary information to enable it to calculate the margin on a gross basis for each indirect client.
- It notes that such issues may be resolved through the recording of indirect clients' positions and collateral value in an individually segregated account (ISA) at the level of the CCP.

As a general comment, we would like to emphasise the need for harmonisation of national insolvency laws in Europe, to the extent possible, in order to effectively support the introduction of pan-European requirements dealing with counterparty defaults such as those being proposed for indirect client clearing under EMIR and MiFIR.

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<ESMA_COMMENT_ RTS_ INDIRECT_CLEARING_1>

Questions from the consultation paper

Q1. Do you agree with the proposed approach to require the choice between an omnibus indirect account and a gross omnibus indirect account with margin at the level of the CCP?

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[In general, we support ESMA's proposal to enhance the resilience of indirect clearing arrangements in light of the concerns highlighted by the industry on the degree of protection of indirect clients' positions. We believe, however, that the proposed solution to offer customers the choice between a net omnibus account and a gross omnibus account structure with margin calculated at the CCP level, will not necessarily provide an equivalent level of protection to that referred to in Article 39 and 48 of EMIR nor simplify the operational set-up of the proposed account models, due to the concerns noted further in the response. We do not believe that the proposed objective of ESMA to reduce operational burden caused by the individual segregated account structure will outweigh the risks of a reduced protection of indirect clients' assets.

As recognised by ESMA, from a segregation perspective, individual segregated accounts provide for the most enhanced form of ring-fencing of client assets from both the clearing members' and all other clients' assets. The gross omnibus account structure, by contrast, does not allow an equivalent level of segregation due to the commingling of positions of the different clients in a single omnibus account. Moreover, the individual segregated structure ensures a higher level of probability of porting in case of default as compared to the gross omnibus structure.

The adequate functioning of a gross omnibus account required under Article 4 (2) (b) of the RTS with position and collateral value calculated for each indirect client in that account at the level of the CCP will heavily rely on the quality of the information that the clearing member will have to pass on to the CCP on a daily basis as required under Article 4 (3) of the RTS. This may give rise to technical difficulties if the information on the single positions of indirect clients required under Article 4 (3) of the RTS is not provided timely or is not sufficiently detailed or accurate; in turn this may give rise to an increased operational risk. The issues described above might increase complexities which could then be replicated across the clearing chain. Such issues may be resolved in the case where an indirect client's positions and collateral value is recorded in an ISA account at the level of the CCP, which we appreciate from ESMA's consultation that it would continue to be a permitted account structure. We would encourage ESMA to also reflect this clarification in the RTS.]

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_1>

Q2. Do you agree with the proposed approach for the requirements related to default management? Do you think there are alternative level 2 requirements (compatible with the relevant insolvency regime situations and the level 1 mandate) that would achieve better protections?

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_2>

[Notwithstanding the comments in response to question 1, were ESMA going to implement the newly proposed account structures, we suggest that the below comments are considered in the final report.

Our understanding is that under paragraph 45 of the consultation, ESMA addresses the issue of treatment of indirect clients in the case of a client default and suggests that such treatment should mirror what is required in Article 48(7) of EMIR in respect to direct clients in the event of a clearing member default. Effectively, in the event of a direct client default, the clearing member should be able to pass the proceeds of the liquidation directly to the indirect clients, if these are known to the clearing member, or to the defaulting client for the account of the indirect clients.

We would like to ask that ESMA clarifies in its final report that our understanding of paragraph 45 is correct and that it is not the intention of the new rules to expect CCPs to perform the leapfrog payments in respect to any indirect clients at any point in the chain. Indeed, in the case of a direct client default or any of its indirect clients, the CCP would act under the instruction of the clearing member, with whom it has a contractual relationship. In the case where both the clearing member and its direct client offering indirect client clearing default, the CCP would still act under article 48(7) of EMIR, therefore returning the liquidation proceeds directly to the direct client of the clearing member, if known, for the account of its indirect clients, or otherwise to the defaulting clearing member for the account of both the direct clients and related indirect clients.]

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_2>

Q3. Do you agree that the proposed approach adequately addresses counterparty risk throughout the longer chain by ensuring an appropriate level of protection to indirect clients? If not, are there alternative approaches compatible with Level 1?

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Q4. For longer chains, what other details (liquidation trigger and steps, flow and content of information, other) should be taken into account or what additional requirements or clarification should be provided in order to avoid potential difficulties when handling the default of a client or an indirect client facilitating clearing services?

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Q5. Do you consider that the new provision assigning by default to the indirect client the choice of an omnibus indirect account following reasonable efforts from the client to receive an instruction is appropriate? If not, what other considerations should be taken into account?

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Q6. Do you consider appropriate that the collateral provided on top of the amount of margin the indirect client is called for is treated in accordance with the contractual arrangements?

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_6>

[Article 4 (4) of both the revised EMIR RTS and the draft MiFIR RTS state that under a gross omnibus account the clearing member shall transfer to the CCP (after applying any haircut) the collateral value received from its client for each indirect client, but not any margin in excess of the clearing member's requirement. However, the rules do not cover the scenario where the margin posted by the clearing member for the account of the indirect client/s is greater than the margin required by the CCP for those indirect client/s. In other words, the rules are silent as to how the CCP should treat any collateral excess received by the CCP from the clearing member for the account of indirect clients. We believe that it would not be appropriate for the CCP to allocate such excess to each indirect client in the account, especially considering that this is not an EMIR requirement for direct clients opting for an omnibus account. Moreover it would be costly for both the clearing members and the CCP to adopt a 'gross omnibus with excess model' because the clearing member would have to inform the CCP, at least daily, of the collateral value of each indirect client, otherwise the CCP would not be able to identify it in an omnibus structure. As a result this model would require additional interfaces between the clearing member and the CCP, not achieving the objective of ESMA's new proposal to reduce the complexity and related cost for indirect client clearing. To address the concerns above, we encourage ESMA to add the below wording to paragraph 4 of Article 4 of both draft RTSs.

New 4(a) Any additional collateral value that is transferred by the clearing member to the CCP above the margin amount called by the CCP should be attributed by the clearing member to each indirect client in its records and accounts. The CCP may record such excess as the clearing member resources for the account of indirect clients.

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_6>

Q7. In view of the different amendments described above, do you consider that this set of requirements ensures a level of protection with equivalent effect as referred to in Articles 39 and 48 of EMIR for indirect clients?

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Q8. Please indicate your answers to the cost-benefit survey?

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Q9. Do you have any comments on the draft RTS under EMIR not already covered in the previous questions?

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_9>

[In the context of the newly proposed gross account structure, we support the introduction of the requirement in article 4(3) in both the revised EMIR RTS and the draft MiFIR RTS under which the clearing member will need to provide the CCP with all the necessary information to identify the positions and the collateral value held for the account of each indirect client in a gross omnibus account. This is critical for the CCP to be able to calculate the margin on a gross basis for each indirect client. As noted in our answer to question 1, the adequate functioning of a gross omnibus account required under Article 4 (2) (b) of the RTS will heavily rely on the quality of the information that the clearing member will have to pass on to the CCP on a daily basis; the lack of timely and sufficiently detailed or accurate information may give rise to an increased operational risk.]

<ESMA_QUESTION_RTS_INDIRECT_CLEARING_9>

Q10. Do you have any comments on the draft RTS under MiFIR not already covered in the previous questions?

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[See response to question 9.]

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