Date 29/01/16

Subject: **FIA Response to the European Commission Consultation**: *"Call for Evidence: EU Regulatory Framework for Financial Services"*

For your consideration

The Commission is looking for empirical evidence and concrete feedback on:

A. Rules affecting the ability of the economy to finance itself and growth;
B. Unnecessary regulatory burdens;
C. Interactions, inconsistencies and gaps;
D. Rules giving rise to unintended consequences.

It is expected that the outcome of this consultation will provide a clearer understanding of the interaction of the individual rules and cumulative impact of the legislation as a whole including potential overlaps, inconsistencies and gaps. It will also help inform the individual reviews and provide a basis for concrete and coherent action where required. Evidence is sought on the impacts of the EU financial legislation but also on the impacts of national implementation (e.g. gold-plating) and enforcement.

**Feedback provided should be supported by relevant and verifiable empirical evidence and concrete examples. Any underlying assumptions should be clearly set out. Feedback should be provided only on rules adopted by co-legislators to date.**

## Executive summary

FIA is pleased to present its response to DG FISMA's Call for Evidence: EU Regulatory Framework for Financial Services.

In summary, our members recommend that:

**Leverage ratio:** Basel Committee and European Commission to amend the leverage ratio in the area of exposure value calculation for client cleared derivatives to recognise the exposure reducing effect of segregated margin – amend leverage ratio methodology to move from CEM to SA-CCR (without modifications) so that it is not punitive to client clearing of derivatives (which, under other pieces of global and EU regulatory reform agenda, is being mandated) and end retail investors (e.g. through pension funds) or market participants with off-setting positions, including amending weightings and other add-ons;

**Indirect clearing:** ESMA to publish final Regulatory Technical Standards (RTS) that enable a scalable model for indirect clearing of OTC and exchange-traded derivatives (ETDs)which addresses insolvency and property law issues contained in earlier RTS proposals under EMIR and MiFIR –limit scope to EU CCPs, EU indirect clients and limited 'length of chains' to the first four parties in a clearing chain, give CMs discretion as to whom to offer indirect clearing; reduce number of accounts required to be set up at a CCP;

**Equivalence Determinations**: it is essential that the Commission proceeds with equivalence assessments under Article 25 of EMIR for key jurisdictions like the US and in advance of other non-EEA CCPs applying to ESMA for recognition to avoid disruptive delays;

**Commodity Firms – Capital:** European Commission should consider a proportionate regime for such firms in order to preserve liquidity and diversity in the marketplace, including proportionate measure for smaller firms – extend existing exemption from certain parts of capital requirements to all parts of the regulations until a proportionate regime is agreed;

**Commodity Firms:** amend position reporting regime for commodity firms – amend Level I text to fix position reporting all the way to the end client or change to end-client reporting.

**Trading and E-Trading:** ESMA to recognise equivalence or substituted compliance of MiFID II rules under CFTC Regulation on Automated Trading – European Commission to permit use of codes other than ISINs (e.g. AIIs), confirm whether third country users of Direct Electronic Access (DEA) have to be authorised as investment firms, and address industry concerns on Systematic Internalisers (SIs) and the use of confidential personal data;

**Reporting:** continue to permit the use of other security identifier numbers besides ISINs e.g. AIIs - move to single-sided trade reporting for OTC derivatives and a complete exemption - further consideration of cumulative impact of the disparate and duplicative reporting regimes under EMIR, MiFIR, MAR, REMIT etc.;

**Definitions:** a number of definitions in various regulations do not provide adequate certainty for firms to understand to what extent regulations apply to them – these definitions should be clarified through changes in the text or through the appropriate guidance, FAQ by the European Commission regarding Level I or Q&A from ESMA in the case of level II;

**Global Solutions:** there should be greater collaboration and coordination with third-country legislators and regulators, and greater regard for consistency in global timelines for implementation of high-level political commitments – Commission to wait for the completion of the CPMI-IOSCO paper on CCP recovery and the FSB paper on resolution prior to formulating its CCP Recovery and Resolution implementation work.

**Response**

[Note to draft: In this section we can provide evidence on the 15 issues set out in the consultation paper. You can give up to 5 examples for each issue. The issues are divided in four themes.]

| |
|---|
| **Theme A. Rules affecting the ability of the economy to finance itself and grow** |

## Issue 1 – Unnecessary regulatory constraints on financing

The Commission launched a consultation in July on the impact of the Capital Requirements Regulation on bank financing of the economy. In addition to the feedback provided to that consultation, please identify undue obstacles to the ability of the wider financial sector to finance the economy, with a particular focus on SME financing, long-term innovation and infrastructure projects and climate finance. Where possible, please provide quantitative estimates to support your assessment.

## Example 1 for Issue 1 (Unnecessary regulatory constraints on financing)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**CRR – LEVERAGE RATIO**

REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 - Capital Requirements Regulation (CRR) - Articles 429-430 (Leverage Ratio)

**Please provide us with an executive/succinct summary of your example:**

EMIR and CRR do not mutually re-enforce the G20 objective of increasing the extent to which derivatives are cleared via CCPs. Whilst EMIR seeks to promote central clearing, the CRR-mandated regulatory capital costs and leverage ratio requirements applicable to central clearing have directly resulted in clearing brokers leaving the industry, thereby reducing access to central clearing. The feedback from our members is that this trend will continue. The key issue here is that the leverage ratio does not currently recognise the exposure-reducing effect of segregated margin for client cleared trades: as a result, clearing members have much less balance sheet capacity to clear derivatives for their clients, which is actively hampering the successful implementation by the industry of the EMIR clearing obligation. This also means that post-default porting may not work as clearing members are not willing to contractually commit to act as a back-up clearing broker because they do not have sufficient balance sheet capacity to do so.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

FIA will be coordinating the submission of data to the Bank for International Settlements (BCBS) in a future data collection exercise in response to the BCBS's monitoring of the Basel rules (https://www.bis.org/bcbs/qis/). The data exercise is an official collection under the Basel Committee's Quantitative Impact Study (QIS) and is usually repeated semi-annually with end-December and end-June reporting dates. We believe this data will be able to evidence the impact of the leverage ratio on the provision of clearing services. We encourage the Commission to discuss the results of the data exercise with the BCBS.

By way of illustration, the following Commodity Futures Trading Commission (CFTC) data illustrate how the US FCM structure and consequently the clearing model changed. The number of FCMs dropped to 73 as of October of 2015. That is compared to 179 in 2005.

| **Table 1** | 2005 | 2010 | 2015 |
|---|---|---|---|
| Number of FCMs | 179 | 126 | 73 |
| Customer Seg Funds (total) | 93.3 | 150.9 | 153 |
| Top 10 FCMs Customer Seg Funds | 61.4 | 117 | 112 |
| Top 10 FCMs Customer Seg Funds % | 65.81% | 77.53% | 73.20% |

http://www.cftc.gov/MarketReports/FinancialDataforFCMs/index.htm

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The leverage ratio should be amended so as to recognise the exposure-reducing effect of segregated margin and SA-CCR should be adopted as a replacement for CEM in the leverage calculation, in order to address the shortcomings of the CEM model (as outlined in BCBS279). This is essential, to ensure that: there is sufficient balance-sheet capacity among clearing brokers to clear the derivatives that are declared subject to mandatory clearing under EMIR, as well as incentivise voluntary clearing of derivatives, and to directly and indirectly support post-default porting.

## Example 2 for Issue 1 (Unnecessary regulatory constraints on financing)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**PROPOSED FINANCIAL TRANSACTION TAX**

Proposal for a Council Directive of 28 September 2011 on a common system of financial transaction tax and amending Directive 2008/7/EC [COM(2011) 594 final - Not published in the Official Journal] – Financial Transaction Tax (FTT).

**Please provide us with an executive/succinct summary of your example:**

The imposition of a financial transaction tax (FTT) would produce harmful effects to both the financial sector and the real economy. The initiative runs counter to the CMU because it will both increase fragmentation and inefficiency. It would first and foremost increase the cost of hedging for end-users, thus acting as a disincentive to manage risk. These increased costs would act as an obstacle to accessing financial markets, restrict liquidity, and ultimately hamper economic growth. It is crucial that cost-benefit analyses be conducted before proposing new regulations that may have harmful effects on the liquidity of the market.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[Please provide data here]

PwC report *'Financial transaction tax: the impacts and arguments'*

Commission Staff Working Document, Economic Analysis, p. 51
1 Oliver Wyman (2013) 'Impact of the EU11 FTT on end-users' report

**Example Sweden**: Sweden implemented its tax in 1984. It was a 0.5% tax on a purchase or sale of an equity security. It was doubled in 1986 and subsequently lowered. In 1991 the tax was abolished following disappointing revenues.

Anders Borg, Sweden's finance minister, explained in an interview to the BBC that a European financial transaction tax won't work, citing his countries own experiment with the tax. When Sweden began taxing financial transactions in the 1980s, "between 90%-99% of traders in bonds, equities and derivatives moved out of Stockholm to London," Borg said. "The impact was basically that we did not get any tax revenue. It brought in very little tax money while moving most of the businesses outside of Sweden. We abandoned [the tax] because it was a very, very bad functioning tax." Borg argues that the countries example should be a lesson to Europe, and that traders would flee to the US or Asia if the tax was implemented.

**Example Italy:** http://www.economist.com/news/finance-and-economics/21641258-new-life-bad-idea-still-kicking - The Economist: Financial-transaction taxes; Still kicking, 31 January 2015.

The article provides details on the French Financial Transaction Tax (French FTT) which is a tax on the purchase of certain French equities. In addition, the impact of the Italian Financial Transaction Tax (Italian FTT) is a tax on certain transactions involving financial instruments issued by companies resident in Italy. The scope of the FTT includes shares, equity-like financial instruments and derivatives, as well as high-frequency trading.

Italian FTT followed the introduction of French FTT and adopted a similar model but with extended scope. In Italy, a sharp fall in volume could be observed. Average trading on all Italian markets since the taxes were put in place was almost 12% lower than in 2012, whereas trading elsewhere in Europe increased by almost 7%. For full details, please see - The Economist : Financial-transaction taxes; Still kicking, 31 January 2015.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The proposal to impose a broad-based financial transaction tax (FTT) will ultimately increase the costs of hedging for large, medium and small corporations and entities, which use derivatives products to manage interest rate, currency, credit and counterparty risks. The introduction of new taxes mean that financial institutions will pass on the additional costs to customers, and this would act as a barrier to accessing financial markets, as well as restricting liquidity and increasing volatility in those markets. A FTT proposal is counter-productive to the aims of the CMU and should be abandoned.

## Example 3 for Issue 1 (Unnecessary regulatory constraints on financing)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

EMIR, MiFID II versus Dodd-Frank Act and CFTC regulation promulgated thereunder

(If applicable, mention also the articles referred to in your example)

DERIVATIVE MARKETS ARE GLOBAL AND REQUIRE GLOBAL SOLUTIONS

**Please provide us with an executive/succinct summary of your example:**

The derivatives markets are global. Any action by the EU that is significantly out of step with actions taken in a coordinated, controlled, fashion by fellow regulators in other major relevant non-EU markets risks causing a fragmentation of liquidity (so hampering the ability of end users to risk manage their exposures as part of their legitimate hedging strategies) and significant market disruption (as users and service providers move their business outside of the EU). As different countries have implemented various regulations at different times, a number of challenges for firms that clear in multiple jurisdictions can be observed.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

- Lack of certainty on how SEF equivalence will work under MiFIR
- Drawn out US CCP recognition process under EMIR – While many foreign CCPs have been recognised as equivalent in Europe, the US and Europe have yet to reach an agreement. This has real consequences for our markets, and ripple effects through the global economy. If equivalence cannot be reached, many EU clearing firms on US markets would have putative capital charges and may have to stop clearing altogether.
- Inconsistent and transparent process used for determining equivalence – role of CPMI/IOSCO principles as a tool for equivalence is inconsistent across dossiers

[Please provide data here]

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

[Please provide suggestions here]

European Commission to deem all US SEFs as equivalent under MiFIR.

More collaboration and coordination with third-country legislators and regulators. The Chicago Federal Reserve conference in November 2015 on CCP resolution was a welcome improvement.

Deference and substituted compliance should be the path forward. Comparable rules and regulations can ensure equivalent regulatory outcomes while reducing the cost of duplicative efforts. The goal should be that the risks of central clearing are both transparent and effectively managed.

If global regulations are not well coordinated, markets could balkanize along regional lines, harming participant access, lessening market liquidity and concentrating risk.

Encouraging is that IOSCO's Cross-Border Task Force has acknowledged these concerns and has put out a tool kit that will help nations reach principles of comity. IOSCO's final report can be found here: http://www.iosco.org/library/pubdocs/pdf/IOSCOPD507.pdf

**Issue 2 – Market Liquidity**

Please specify whether, and to what extent, the regulatory framework has had any major positive or negative impacts on market liquidity. Please elaborate on the relative significance of such impact in comparison with the impact caused by macroeconomic or other underlying factors.

## Example 1 for Issue 2 (Market Liquidity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

LACK OF EQUIVALENCE DETERMINATIONS

REGULATION (EU) No 648/2012 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 4 July 2012 on OTC derivatives, central counterparties and trade repositories – European Market Infrastructure Regulations (EMIR) – Article 25 (Equivalence), Article 13 (Equivalence)

**Please provide us with an executive/succinct summary of your example:**

EMIR - Article 25 (Equivalence)

European firms will face higher capital requirements when transacting with a CCP that is not recognised (or authorised) under EMIR – the current recognition process means that European market participants are uncertain about the regulatory status of many third country CCPs, and their consequent ability to engage in these markets.

If equivalence determinations for the outstanding jurisdictions like the US are not forthcoming, EU firms may not be able to clear derivatives on CCPs located in such jurisdictions (even indirectly) and, in any event, will incur onerous capital requirements if they continue to access third-country CCPs that have not been recognised – this would likely lead to such firms ceasing to access those third-country CCPs, resulting in a fragmentation in liquidity.

EMIR – Article 13 (Equivalence)

EMIR provides for a mechanism whereby certain transactions between entities which are consolidated on the same balance sheet, where one entity is established in a third country which has been subject to an equivalence determination by ESMA and adopted by the Commission, would be deemed to have fulfilled the obligations contained in Articles 4, 9, 10 and 11 of EMIR. However, the Commission has not adopted any such equivalence determinations.

It is not clear how Article 13 applies where an EU entity enters into a derivative contract through a non-EU branch and that branch is located in a jurisdiction with equivalent rules (and is subject to those rules) but the counterparty is located in a third jurisdiction (and similar issues apply in relation to non-EU entities that are entering into transactions with an EU counterparty where the non-EU entity is acting through a branch in an equivalent jurisdiction and is subject to the rules in that jurisdiction).

While there has been some limited clarification of these issues by ESMA, it is unsatisfactory that these important issues are not explicitly resolved by the Level 1 text.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[Please provide data here]

ESMA's Steven Maijoor criticised the extremely rigid and burdensome process, and that equivalence decisions were taking much more time than expected.

Keynote Speech Steven Maijoor – Clearing the way towards an OTC derivatives union

http://www.esma.europa.eu/system/files/2015-1417_steven_maijoor_isda_europe_conference_speech_2015.pdf

ESMA – EMIR Review Report No 4 pp 19-21 – http://www.esma.europa.eu/system/files/esma-2015-1254_-_emir_review_report_no.4_on_other_issues.pdf

*Pp 20 – Para 105 - The process for the recognition of TC-CCP is extremely rigid and burdensome, as demonstrated by the limited number of recognition decisions taken so far. The equivalence decision process is taking much more time than expected. ESMA delivered its technical advice in September and October 2013 and as of today the equivalence determinations covered only a limited number of countries. Three years after the entry into force of EMIR, the majority of the TC-CCPs are still operating under a transitional regime. This puts at risk European clearing members and their subsidiaries clearing with these TC-CCPs and creates the potential for regulatory arbitrage between European and third country CCPs.*

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

**EMIR Article 25 -** The EMIR Art 25 process needs to be more transparent and forthcoming and be granted in a timely manner.

It is essential that the Commission proceeds with reaching an equivalence decision on the US soon and in any case ahead of mandatory clearing under EMIR going live in June 2016.

Equivalence assessments for other key jurisdictions (e.g. Brazil, India, etc.) should be delivered in a timely manner and in advance of CCPs applying to ESMA for recognition under EMIR Article 25 to avoid disruptive delays.

The outcome-based approach to equivalence applied by the Commission to numerous jurisdictions to date ought to be used in all cases, as rules at a national level will always differ at a granular level.

If resource-intensive equivalence and recognition procedures are to be put in place, flexible transitional arrangements are needed. It is not appropriate that non-EU markets are impacted by EU deadline or delays in completing determinations. The EU approach should also have some flexibility to make adjustments on the basis of international developments.

**EMIR Article 13 -** FIA members recommend that the treatment of branches of EU/non-EU entities be clarified in the level 1 text. This should be the subject of a specific consultation to ensure that the proposed changes are appropriate. In particular, the changes should specifically address how the provisions of Article 13 apply in relation to entities acting through branches to ensure appropriate relief from duplicative and conflicting rules.

## Example 2 for Issue 2 (Market Liquidity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

CRR – LEVERAGE RATIO

CRR - Articles 429-430 (Leverage Ratio)

**Please provide us with an executive/succinct summary of your example:**

EMIR and CRD IV do not mutually re-enforce the G20 objective of increasing the extent to which derivatives are cleared via CCPs. Whilst EMIR seeks to promote central clearing, the CRD IV-mandated regulatory capital costs and leverage ratio requirements applicable to central clearing have directly resulted in clearing brokers leaving the industry, thereby reducing access to central clearing. The feedback from our members is that this trend will continue. The detrimental effect of the regulatory capital and leverage ratio requirements imposed on clearing members pursuant to the CRR. The key issue here is that the leverage ratio does not currently recognise the exposure-reducing effect of segregated margin: as a result, clearing members have much less balance sheet capacity to clear derivatives for their clients, which is actively hampering the successful implementation by the industry of the EMIR clearing obligation.

Furthermore, the leverage ratio not only acts to constrain the ability of clearing brokers to take on new clients in business-as-usual circumstances, but will also affect the ability of clearing brokers to absorb additional capacity under post-default porting arrangements in the case of another clearing broker's default. In other words, clearing brokers will not have balance sheet capacity to service liquidity and clients in a post-default porting situation.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[Please provide data here]

- Bank regulation has increasingly placed constraints on the balance sheet capacity of banks to act in the clearing space – indeed, in October 2015 at a conference in Hong Kong, Commodities Futures Trading Commission (CFTC) commissioner Chris Giancarlo called for a fundamental review of the approach to prudential capital by banking regulators. One particular issue which has blighted banks in the treatment of exposures to collateral posted by clients as initial margin.

- FIA will be coordinating the submission of data to the Bank for International Settlements (BIS) in a future data collection exercise in response to the Basel Committee's Banking Supervision (BCBS) monitoring of the Basel rules (https://www.bis.org/bcbs/qis/). The data exercise is an official collection under the Basel Committee's Quantitative Impact Study (QIS) and is usually repeated semi-annually with end-December and end-June reporting dates. We believe this data will be able to evidence the impact of the leverage ratio on the provision of clearing services. We encourage the Commission to discuss the results of the data exercise with the BCBS.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The leverage ratio should be amended so as to recognise the exposure-reducing effect of segregated margin and that SA-CCR be adopted as a replacement for CEM in the leverage calculation, in order to address the shortcomings of the CEM model (as outlined in BCBS279). This is essential, to ensure that: there is sufficient balance-sheet capacity among clearing brokers to clear the derivatives that are declared subject to mandatory clearing under EMIR.

## Example 3 for Issue 2 (Market Liquidity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**MiFID II / MiFIR - TRANSPARENCY**

REGULATION (EU) No 600/2014 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 – Markets in Financial Instruments Regulation (MiFIR) – Articles 8-11 and 18-21 (Non-Equity Transparency)

**Please provide us with an executive/succinct summary of your example:**

It is important to calibrate pre-transparency requirements adequately so as not to dissuade provisions of liquidity to markets.

FIA is in favour of greater transparency in derivatives, which we believe will promote further growth and improve liquidity, but the thresholds for determining whether derivatives should be traded on a trading venue and subject to pre- and post-trade transparency under MiFID/MiFIR should be appropriately calibrated. If derivatives which are not sufficiently liquid in practice are subjected to the trading obligation and transparency requirements, there is a real risk that the requirements could make it near impossible for market-makers to safely provide liquidity and hedge themselves, which in turn could result in a severe drop off in liquidity in Europe in those products.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[Please provide data here]

More time is required to provide data based on a detailed analysis.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Calibrate transparency requirements adequately and provide provisions for packages for pre-trade transparency requirements.

## Example 4 for Issue 2 (Market Liquidity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**GENERAL OBSERVATIONS ON LIQUIDITY, i.e. MiFID II, CRR**

**Please provide us with an executive/succinct summary of your example:**

A well-functioning market must be underpinned by sufficient liquidity for there to be consistent observable prices, narrow spreads and the ability to execute transactions or a series of transactions or strategies. It should be noted that the availability of liquidity stems from the presence of a range of different market participants. There are concerns that efforts to increase transparency without giving regard to the effects on the markets may remove the incentive for participants to be active in the market, and are feared to have detrimental effects on liquidity. The EC should consider this in the context of considering introducing further regulation and/or other regulatory measurements.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Reference to the Financial Times Article – "Investors will pay if liquidity dries up" – 12 November 2015

http://www.ft.com/cms/s/0/2964df72-8914-11e5-9f8c-a8d619fa707c.html#axzz3yMw2mLxO

*"[…] Even a temporary dislocation will push up borrowing costs, which could create cash flow problems for borrowers."*

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The EC should prioritise liquidity, as greater liquidity results in markets which are less easily manipulated, and consequently regulators should afford market participants the tools with which to foster liquidity. We do not believe that an 'oversupply' of liquidity can be detrimental to markets, but the supply of liquidity without appropriate risk management can be imprudent.

## Issue 3 – Investor and consumer protection

Please specify whether, and to what extent, the regulatory framework has had any major positive or negative impacts on investor and consumer protection and confidence.

FIA proposes not to respond to this section

## Issue 4 – Proportionality / preserving diversity in the EU financial sector

Are EU rules adequately suited to the diversity of financial institutions in the EU? Are these rules adapted to the emergence of new business models and the participation of non-financial actors in the market place? Is further adaptation needed and justified from a risk perspective? If so, which, and how?

### Example 1 for Issue 4 (Proportionality / preserving diversity in the EU financial sector)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

ACCESS TO CENTRAL BANK LIQUIDITY AND CCP INVESTMENT POLICY

EMIR RTS 153/2013

**Please provide us with an executive/succinct summary of your example:**

Article 47 (Investment Policy) of EMIR, as supplemented by Article 45(2) of RTS 153/2013 (Highly secured arrangements maintaining cash), requires that not less than 95% of all cash balances maintained overnight other than with a central bank shall be deposited through arrangements that ensure the collateralisation of the cash with highly liquid financial instruments meeting the EMIR requirements.

In practice, this means that CCPs that cannot deposit their cash at a central bank have to reverse repo out almost all the cash that they would otherwise hold overnight. Article 44 accordingly imposes a stringent obligation on European CCPs to have access to deep and liquid commercial repo markets.

This requirement introduces a material degree of circularity in respect of the CCP's credit and liquidity risk exposures - over the course of any given trading day, banks (through their OTC clearing or exchange traded derivatives (ETD) desks) provide collateral to the CCP in order to protect the CCP against the default of such bank, only for the CCP to hand back such collateral to another part of that bank (the repo desk):

- The liquidity of a CCP originates from its clearing members: each day, clearing members provide collateral in cash and non-cash form to the CCP, to protect the CCP against the default of such clearing members.
- The settlement agents used by the CCP to settle payments (of margin and otherwise) are often the same financial institutions as the clearing members: if that clearing member defaults, for example by reason of its insolvency, such clearing member will also cause significant liquidity issues for the CCP (because one of its settlement agents will also be in default), if they are less able to transfer assets between them and their clearing members.

- The largest players in the commercial repo markets are typically the larger clearing members of such CCP. Accordingly, if a clearing member defaults, it is also likely to result in a default under one or more repo facilities established with that CCP pursuant to Article 44 of EMIR.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Repos have a much higher default risk than exposures to central banks. As noted in a BIS report published shortly after the 2008 crisis: "Whereas fails to deliver Treasuries had averaged around USD90 billion per week during the two years preceding the crisis, they rose to above USD1 trillion [per week] during the Bear Sterns episode and then soared to record higher of almost USD2.7 trillion [per week] following the Lehman default. The extraordinarily low GC repo rates during this period exacerbated the problem by reducing the cost of failing. Normally, the failing party would borrow the necessary security through a reverse repo to avoid failing. But when repo rates are close to zero, the interest rate earned overnight is below the cost to borrow the required securities, there is no incentive to avoid failing (Fleming and Garbade (2005)). As settlement fails increased, investors who had previously lent out their Treasuries pulled back from repo markets, as the low GC rates available were not enough to compensate for the risk that the securities might not come back. These dynamics have been recognised by the Treasury Market Practices Group, a body of market participants convened by the Federal Reserve Bank of New York". Whilst the situation in European repo markets on that occasion was not the same as the US repo markets, the occurrence of the above events in the European repo markets in a future stressed scenario cannot be precluded. Article 45(2) of RTS 153/2013 effectively forces CCPs to be exposed to the credit and liquidity issues highlighted in the above referenced article. This is not a desirable regulatory outcome: the key objective must be to ensure that the assets of the CCP are exposed to as little credit and liquidity risk as possible, given their heightened importance in the global financial system following the 2009 G20 Commitments.

It has been questioned whether the repo markets have sufficiently deep liquidity to meet the increasing demands of CCPs pursuant to EMIR. The above article highlights how quickly such liquidity can dry up. In June 2015, the Financial Times reported that the Chief Risk Officer of LCH.Clearnet (the world's largest interbank swaps clearer) has expressed concern that LCH.Clearnet may soon reach a threshold where it would have to stop accepting new trades for clearing, as it would become untenable for the CCP to invest through the repo markets on a daily basis the approximately USD150 billion of client funds that it holds. The extent to which there will be sufficient liquidity in the repo markets with respect to certain non-G7 currencies to enable CCPs to meet their EMIR reinvestment obligations is also uncertain.

The increasing demand for repo services by CCPs, combined with the increase in regulatory capital costs for those banks who provide such repo services, can reasonably be anticipated to increase costs for all users of commercial repo services:

- one can envisage that, in time, Article 45(2) of RTS 153/2013 may have unintended knock-on consequences for other (non-CCP) users of the commercial repo markets: as CCPs' demand for access to commercial repo markets continues ever upward, there is a risk that the availability of repo facilities for non-CCP users of European markets decreases; and
- the absolute availability of repo facilities may also decrease in coming years: the ability of banks to provide commercial repo facilities (to CCPs and non-CCPs alike) is also increasingly constrained, by

reason of the introduction of further constraints on banks' balance sheets under Capital Requirements Directive IV ("CRDIV") with respect to their commercial repo businesses.

Finally, Article 45(2) of RTS 153/2013 has proven impractical to comply with for CCPs in respect of accounts whose investment is segregated, where relatively small amounts of particular currencies are collected. It is not commercially possible to engage in reverse repo transactions (investing cash for non-cash) in the financial markets for small amounts of currency. The response of some CCPs has been to cease allowing cash margin to be provided for particular accounts. This has reduced clearing member choice as to collateral and eliminates the possibility of margin calls on public holidays in the country of the currency being called. In practice, this requirement has reduced demand for usage of European currencies by US clearing members and their customers.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

- Article 33(1)(a) of Regulatory Technical Standards (RTS) 153/2013 should be amended, so that deposits in currencies other than the applicable central bank's currency of issue count as part of the CCP's liquid resources;
- An exception for relatively small amounts of currency, linked to the commercial viability of reverse repo programmes, should be introduced or Article 45(2) of RTS 153/2013 should be amended to clarify that the 95% reinvestment rule applies across all cash held by a CCP and not on a per currency per account basis.
- The typographical error in the closing words of Article 45(2) of RTS 153/2013 should be amended, so as to read "the requirement under Article 43, except the requirement at paragraph 1(c) of Annex *II*."

RTS 153/2013, Article 45(2) should be amended to read:

- "2. Where cash is maintained overnight in accordance with paragraph 1 then not less than [95]% of such cash, calculated over an average period of one calendar month *and measured on a cumulative basis across all accounts and currencies*, shall be deposited through arrangements that ensure the collateralization of the cash with highly liquid financial instruments meeting the requirements under *Article 43*, except the requirement at paragraph 1(c) of *Annex II*".

## Example 2 for Issue 4 (Proportionality / preserving diversity in the EU financial sector)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**MiFID II – Article 2 (Exemptions) / CRR – various, but in particular Articles 493 and 498 (Commodity 'Dealer' Exemption)**

**Please provide us with an executive/succinct summary of your example:**

Due to a change in scope of MiFID II / MiFIR, and the inability of some firms to rely on an ancillary activity exemption for their hedging activities, a number of commodity firms will fall into scope of MiFID, many for the first time. By being classified as investment firms under MiFID II, such commodity firms would become subject to a number of conduct related requirements under MiFID II/ MiFIR, REMIT and MAD, as well as also falling into scope of the Capital Requirements Regime (CRD IV and CRR), which imports significant obligations related to the own funds, liquidity and exposures that such firms can maintain.

Many commodity firms have 'native' exposure (i.e. being long the underlying) to risk in commodities but do not principally speculate in price movements - most trading tends to be for the purposes of hedging such native exposures. Moreover, the Capital Requirements regime was introduced to prevent banks which principally employ leverage to extend credit to a wide number of counterparties, whereas commodity firms do not pose the same systematic risks, nevertheless, such firms are an important source of liquidity for commodity markets, driving the real economy and the creation of jobs and growth.

Consequently, the application of the Capital Requirements regime to commodity firms has a disproportionate effect on the returns generated by these firms, which in turn is causing a number of firms to consider relocating to other jurisdictions in Asia and the US.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Reference is made to the joint FIA Europe – EFET and ISDA letter (dated 17 July 2015) on the potential impact of extending the capital requirements regime to commodity firms, the position paper is available here: https://fia.org/articles/fia-europe-efet-and-isda-joint-position-paper-capital-regime-commodities

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Consider a more appropriate and proportionate approach to regulation of commodity firms.

FIA members support the Commission's current legislative proposal to extend the commodity dealer exemption in Art 493 and 498 of CRR to December 2020.

Please refer to the joint FIA Europe – EFET and ISDA letter (dated 17 July 2015) on the potential impact of extending the capital requirements regime to commodity firms, the position paper is available here: https://fia.org/articles/fia-europe-efet-and-isda-joint-position-paper-capital-regime-commodities

## Example 3 for Issue 4 (Proportionality / preserving diversity in the EU financial sector)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**EMIR Article 49 (Review of Models, Backtesting and Stress Testing) and Article 15 (Extension of Services)**

**Please provide us with an executive/succinct summary of your example:**

EMIR Article 49 provides requirements for CCPs to obtain independent validation and inform its NCA and ESMA of any changes before adopting any significant change to a CCPs' models and parameters.

The current college system is not transparent in relation to when a proposed new product or service, or change to a CCP's model, backtesting and stress testing frameworks will be subject to college review. There is also a lack of transparency about the information and documentation required under the Article 49 process, and in particular regarding the timeframe and progress of an application in accordance with the Article 49 college process.

i. **Review of models, backtesting and stress testing**

The current process for the review of models, backtesting, and stress testing, should be reviewed as it is not explicitly clear when the review process is triggered or how the various steps in the process interact.

At present, there is a divergence of practice amongst national authorities as to when changes to a CCP's models, backtesting and stress testing frameworks are considered to be 'significant' and therefore trigger a more in-depth the review process. Once the process is triggered there appears to be a duplication of process with the CCP, national authority, and ESMA all undertaking a validation of the model and parameter changes. We believe this duplication of process is unduly onerous, and results in unnecessary delays for CCPs in implementing such changes, and hampers their ability to provide innovative risk management solutions to the marketplace. We would request a simplification of the process for having changes to a CCP's models, backtesting and stress testing frameworks approved, and in particular the removal of the duplicative elements of the current process.

**ii. Extension of EMIR Authorisation under Article 15 of EMIR**

The issues under EMIR Article 15 are related. The current process for the extension of a CCP's authorisation under Article 15 should be reviewed as it is not explicitly clear when an extension is required.

At present, there is a divergence of practice amongst national authorities as to when the commencement of a new product or service is considered to be 'additional' and therefore trigger the review process for an extension of a CCP's authorisation. There is no clear definition of "additional services and activities" in EMIR, which has resulted in national authorities having taken differing interpretations of the scope of a CCP's original authorisation.

National authorities interpret the college review provisions differently. There is no definition of "additional services and activities" in EMIR, which has resulted in divergence at the national level.

The current college methodology should be reviewed as it is unpredictable as to when the college review process is triggered and how the process will unfold.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

Currently, college reviews have an opaque timeframe, which means delays and causes uncertainty around product launches, making it difficult to take informed business decisions. This causes an adverse effect, hampering CCPs' abilities to provide new risk management solutions to the marketplace.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Enhanced transparency around the college process, and the introduction of a timeframe for decisions, and an increase in the frequency of college meetings to ensure bottlenecks are avoided.

**Theme B. Unnecessary regulatory burdens**

## Issue 5 – Excessive compliance costs and complexity

In response to some of the practices seen in the run-up to the crisis, EU rules have necessarily become more prescriptive. This will help to ensure that firms are held to account, but it can also increase costs and complexity, and weaken a sense of individual responsibility. Please identify and justify such burdens that, in your view, do not meet the objectives set out above efficiently and effectively. Please provide quantitative estimates to support your assessment and distinguish between direct and indirect impacts, and between one-off and recurring costs. Please identify areas where they could be simplified, to achieve more efficiently the intended regulatory objective.

## Example 1 for Issue 5 (Excessive compliance costs and complexity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**MiFID II Reporting Obligations/EMIR – Reporting Obligations/SFTR reporting Obligations and Market Abuse Regulation**

Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency – **REMIT – Reporting Obligations**

Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on reporting and transparency of securities financing transactions and amending Regulation (EU) No 648/2012 – Securities Financing Transaction Regulations – **SFTR – Article 4 (Reporting Obligation)**

Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC – **Market Abuse Regulation (MAR) – Reporting Obligations**

**Please provide us with an executive/succinct summary of your example:**

Regulators have become increasingly reliant on the reporting of specific information in order to monitor market abuse, systemic risk and suspicious trading patterns – however, regulation has been implemented in an increasingly fragmented and piecemeal approach which has resulted in duplicative and complex reporting requirements, with firms submitting a number of different report to a number of trade repositories (whether commercial enterprises or ‘public utility’). Simultaneously, regulators struggle to collate data, collecting the wrong data, or using data collected for a purpose other than what it was meant for. Moreover, constant fine-tuning and tweaking to existing systems, and multiple workstreams dealing with a number of different regulations, results in disproportionate costs for firms.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[provide data here]

1% matching rate for ETD EMIR reporting. ESMA states that of the 16 billion EMIR reports >1 billion are unmatched ETD as of 29 May 2015, https://www.esma.europa.eu/news/ESMA-fosters-derivatives-market-transparency?t=326&o=home

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

A holistic view of reporting should be taken, with regulators consolidating the reporting requirements into a single regulation. This should aim at streamlining and simplifying existing burdens, and regulators should also seek to give granular levels of guidance on the data they expect to receive.

## Example 2 for Issue 5 (Excessive compliance costs and complexity)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**MiFID II / MiFIR – Transparency**

**Please provide us with an executive/succinct summary of your example:**

For post-trade reporting under MiFIR's Transparency requirements, investment firms and Systematic Internalisers will have to conduct their own liquidity assessments in order determine liquid products that are reportable to either NCAs or ESMA directly.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[provide data here].n/a

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

ESMA should be required to provide a determinative list of liquid versus illiquid products which could be relied upon by market participants (Golden source).

## Issue 6 – Reporting and disclosure obligations

The EU has put in place a range of rules designed to increase transparency and provide more information to regulators, investors and the public in general. The information contained in these requirements is necessary to improve oversight and confidence and will ultimately improve the functioning of markets. In some areas, however, the same or similar information may be required to be reported more than once, or requirements may result in information reported in a way which is not useful to provide effective oversight or added value for investors.

Please identify the reporting provisions, either publicly or to supervisory authorities, which in your view either do not meet sufficiently the objectives above or where streamlining/clarifying the obligations would improve quality, effectiveness and coherence. If applicable, please provide specific proposals.

Specifically for investors and competent authorities, please provide an assessment whether the current reporting and disclosure obligations are fit for the purpose of public oversight and ensuring transparency. If applicable, please provide specific examples of missing reporting or disclosure obligations or existing obligations without clear added value.

## Example 1 for Issue 6 (Reporting and disclosure obligations)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**EMIR – Reporting Obligations**

**Please provide us with an executive/succinct summary of your example:**

Given that derivatives markets are global, it is critical that the regulatory framework applicable to them is globally consistent, whilst also leaving room to address more regional market issues. The G20 Commitments have been implemented locally in an inconsistent manner, at different paces. Inconsistent methodologies have been applied by Europe when determining whether or not to recognise third-country regulation as being "equivalent" to European regulation. The equivalence process itself is opaque, with little objective guidance provided to help third-country regulators determine whether, and how, their regulations will be deemed sufficient for equivalence to be granted.

Because ETD were added in late to EMIR, a number of fields which are applicable to OTC derivatives are not appropriate for ETDs and therefore industry has been forced to effectively manufacture values for these fields.

Using transaction data to recreate position data outside of a trading system is extremely problematic and difficult to achieve - in any event, aggregation of transactions by regulators to recreate a position is unnecessary when position data is readily available from Regulated Markets, CCPs and Clearing Brokers.

The easiest way to mitigate the risks of regulatory arbitrage and to ensure internationally coherent regulation is to:

- agree sufficiently granular global standards;
- move forward on the same timetable as our immediate peers;
- implement regulation in a consistent manner globally; and

- have the means to pro-actively identify regulatory conflicts and overlaps.

Regulators and legislators should ensure that rules reflect differences between ETD and OTC derivatives. In addition, regulators should move to single sided position reporting for ETD and single sided transaction reporting for OTC derivatives.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Field 14 – Notional Value – ETD are traded in lots of contracts rather than notional values and is therefore not applicable

Field 47 – Effective Date – ETD do not have effective dates. This is a term used in the ISDA Definitions for use with certain OTC derivatives.

Field 11 – Compression – all ETD transactions are compressed into a position. This field was meant to show where an OTC transaction was the result of a compression exercise

Field 28 – Mandatory Clearing – by definition, all ETDs are cleared

Fields 33-40 (interest rate derivatives) – all fields relate to the underlying of the interest rate derivate transaction – these are not relevant for ETD

Fields 45-54 – in line with the last entry, there are a large number of underlying fields that are required to be populated that are not relevant ETD, specifically in the commodities space

[provide data here]

A practical example from the reporting obligation for Special Purpose Vehicles (SPV)

Where an FC and an NFC (specifically, a SPV) have entered into an OTC derivative, imposing the reporting obligation on both parties creates a significant administrative reporting burden on the NFC.

By way of example, an entity with no employees, the SPV is required to delegate the performance of the reporting obligation (typically to the corporate services provider). This necessitates the negotiation of, and entry into a new reporting agreement, which can involve seeking the consent of the other transaction parties (generally, the SPV must seek the consent of the trustee on the basis that entering into the reporting agreement is not materially prejudicial to the interests of the noteholders).

To illustrate further:

1. Corporate Services ("CS") is a business unit within Issuer Services which supplies administrative services to SPVs;

2. By way of example, the CS department located in Dublin ("CS Dublin") provides administrative services to SPVs;

3. Approximately 270 of these SPVs entered into OTC derivatives in connection with issuing debt instruments;

4. Overall, these 270 SPVs had entered into OTC derivatives with approximately 35 different swap counterparties (counting different branches of the same Financial Counterparty as the same swap counterparty);

5. In this regard, the transaction documents for 270 SPVs were reviewed to see if there was any impediment to the SPV entering into an EMIR reporting agreement. This takes on average two hours per SPV;

6. In addition, the terms of the reporting agreements had to be negotiated with the various counterparties. Due to different branches and departments of these counterparties using different forms of reporting agreements, we would estimate that approximately 50 different reporting agreements were used. The negotiation of these agreements usually took three to four weeks but in some cases stretched over several months;

7. Generally, the position arrived at was that the SPV would report its Counterparty Data to the trade repository and the Financial Counterparty would report its Counterparty Data and the Common Data to the Trade Repository;

8. As SPVs have no employees, it fell to CS Dublin as corporate services provider to report the SPV's Counterparty Data. In this regard it was necessary to put a side letter to the corporate services agreement in place between each SPV and CS Dublin;

9. The above steps took several months to complete and, as outlined above, we do not think that it resulted in an improvement in reporting.

FIA members appreciate and support the fact that moving to position reporting will require a different set of reporting attributes. Figures published by ESMA illustrate that since reporting went live on 12th February 2014, around 16 billion transactions have been reported to trade repositories.

FIA and its members were represented on a cross-trade association working group to develop a single-sided reporting hierarchy blueprint for exchange traded and OTC derivatives – see ISDA's response. FIA members are supportive of this proposal.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Adopt Single Sided Position Reporting (SSR): Should the Commission not agree that ETD should be removed from the EMIR reporting regime, then we recommend such ETD reporting regime be amended to become an "end-of-day" single sided position reporting regime. Under EMIR, firms are currently required to report ETDs at a transaction level. However, ETD are managed and valued at a position level.

It should be noted that:

- many CCPs and large brokers run netting cycles at the end of each business day, but not intra-day;
- brokers execute a cross and "hold" the position intra-day, before allocating the trade to the relevant end customer at a later point in time; and
- unlike trades executed via a Central Limit Order Book (CLOB) (which can be reported almost immediately), the speed with which it is possible to report block trades that are executed and become binding over a telephone is inherently slower.

For these reasons, to require positions to be reported intra-day would give a misleading impression of the open interest in such positions. Intra-day reporting would also result in gross positions being reported, to the extent that such positions are not netted until the end of such business day. We therefore consider it more appropriate to report the positions that exist at the end of each trading day, once all block trades are reported to the trading venue and all give-ups / take-ups are finalised.

Using transaction data to recreate position data outside of a trading system is extremely problematic and difficult to achieve - in any event, aggregation of transactions by regulators to recreate a position is unnecessary when position data is readily available from Regulated Markets, CCPs and Clearing Brokers.

A switch to single sided position reporting would not only give regulators the information required to fulfil their mandate, but would also reduce reporting levels by billions of line items a year, thereby significantly reducing costs and operational risk.

If the Commission do adopt this proposal in lieu of excluding ETDs from all reporting obligations under EMIR, we recommend that (i) the CCP be the reporting party for trades between the CCP and the Clearing Broker, (ii) the clearing broker be the reporting party for trades between the clearing broker and its direct clients and (iii) for each back to back contract further down the contract chain that exists between the CCP and the ultimate end user, the party nearest to the CCP be the reporting entity, as set out below.

Party 1 Party 2 Reporting Party
CCP Clearing Member CCP
Clearing Member Direct Client Clearing Member
Direct Client Indirect Client Direct Client
Indirect Client Indirect Client's client Indirect Client
Etc.

Today's "delegated reporting" regime is, in effect, SSR. FIA's proposal effectively seeks to mandate delegated reporting for ETDs at a position level. Those clearing member firms who already offer a delegated reporting service for their clients inform us that there are few material costs per se in moving to single sided position reporting. The main costs relate to (i) the decommissioning of their existing delegated reporting set up and (ii) creating the hierarchy of who has the reporting obligation under SSR.

Like other reporting regimes, collateral and valuations should be reported by the more sophisticated party. The reconciliation of valuation data is dealt with elsewhere in EMIR (e.g. the EMIR portfolio reconciliation provisions);

Single Sided Transaction Reporting: For all other derivatives, we consider that single sided transaction reporting is more appropriate than dual sided reporting. Any dispute as to the accuracy of the trade report could be reconciled through dispute and reconciliation protocols under EMIR Article 11. By way of further proposals relating to reporting under EMIR, FIA recommends that:

-given the significant build out costs for corporates to implement an EMIR reporting process, the general lack of systemic importance and the weak cost/benefit analysis for the same (given they may only enter into a couple of trades a year and are not systemically important users of derivatives), the Commission to consider removing NFC- from the EMIR reporting obligation;
- notwithstanding the move to single-sided reporting / the exemption of ETDs reporting going forward, the reconciliation of outstanding historic unmatched trades should still be completed;

- the requirement to backload the reporting of OTC derivatives transactions should be dropped – there may not be LEIs for historic counterparties;

-differences in the specified labels for and parameters of reporting fields should be harmonised internationally: they currently create unnecessary confusion, leading to perceived errors, and operational costs; and

-for ETDs, the trading venue should be required to publicly specify the UPI applicable to each of the products capable of execution on such venue or pursuant to the rules of such venue.

## Issue 7 – Contractual documentation

Standardised documentation is often necessary to ensure that market participants are subject to the same set of rules throughout the EU in order to facilitate the cross-border provision of services and ensure free movement of capital. When rules change, clients and counterparties are often faced with new contractual documentation. This may add costs and might not always provide greater customer/ investor protection. Please identify specific situations where contractual or regulatory documents need to be updated with unnecessary frequency or are required to contain information that does not adequately meet the objectives above. Please indicate where digitalisation and digital standards could help to simplify and make contractual documentation less costly, and, if applicable, identify any obstacles to this happening.

## Issue 8 – Rules outdated due to technological change

Please specify where the effectiveness of rules could be enhanced to respond to increasingly online-based services and the development of financial technology solutions for the financial services sector.

## Example 1 for Issue 8 (Rules outdated due to technological change)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**Various – EMIR, MiFID II / MiFIR, Settlement Finality Directive**

**Please provide us with an executive/succinct summary of your example:**

In general, the vast amount of regulatory change seen in the past few years (e.g. EMIR, MiFID II / MiFIR) and even more significantly in cases for firms registered in multiple jurisdictions, regulatory change has added significant burdens on firms' existing operational systems. In many cases, those systems were not built to handle those additional functionalities required by regulation.

We are aware that firms are investing heavily in 'blockchain' technology – blockchain technology is viewed as a significantly innovative development and will likely result in operational and cost efficiencies for firms.

http://www.efinancialnews.com/story/2015-09-30/meet-the-blockchain-start-ups-symbiont-clearmatics-setl-eris

Financial News – Meet the new kids on the blockchain

*Server-based applications are expensive to maintain because lots of hardware and staff are needed to run and manage the databases that underpin them. Being centralised, they are also easier to tamper with. Distributed applications are instead run and maintained by a network of computers on the internet. Changes to their databases can be made only by parties on the network who have cryptographic keys and a complex mathematical process ensures changes are irreversible. This could help organisations save money, ensure the integrity of their data and make their processes more efficient.*

http://www.efinancialnews.com/story/2015-09-29/blockchain-the-right-solution-at-the-right-time?mod=emailinfo-mostread

Blockchain: The right solution at the right time?

*Consultancy Aite Group noted in a report in September that some banks were being vague about their initiatives in blockchain, not because they "deem this a trade secret; the simple and harsh reality is that the banks themselves are not clear on how this technology will evolve and ultimately be adopted". Aite estimates banks and other firms operating in the capital markets will spend $400 million a year on developing the blockchain by 2019.*

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

[provide data here]

http://www.ft.com/cms/s/2/eb1f8256-7b4b-11e5-a1fe-567b37f80b64.html#axzz3rO4uzAYf

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Whilst it is too early to regulate this technology, regulators and legislators should be aware that the widespread adoption of blockchain technology is set to underpin and reinvent securities execution, trading, clearing and settlement. Consequently, most major regulations (EMIR, MiFID II/ MiFIR) and other new regulations will have to consider the widespread use of technology.

## Issue 9 – Barriers to entry

Please document barriers to market entry arising from regulation that the EU should help address. Have the new rules given rise to any new barriers to entry for new market players to challenge incumbents or address hitherto unmet customer needs?

## Example 1 for Issue 9 (Barriers to Entry)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**LACK OF EMIR EQUIVALENCE DETERMINATIONS UNDER ARTICLE 25**

REGULATION (EU) No 648/2012 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 4 July 2012 on OTC derivatives, central counterparties and trade repositories – European Market Infrastructure Regulations (EMIR) – Article 25 (Equivalence)

**Please provide us with an executive/succinct summary of your example:**

European firms will face higher capital requirements when transacting with a CCP that is not recognised (or authorised) under EMIR – the current recognition process means that European market participants are uncertain about the regulatory status of many third country CCPs, and their consequent ability to engage in these markets.

If equivalence determinations for the outstanding jurisdictions like the US are not forthcoming, EU firms may not be able to clear derivatives on CCPs located in such jurisdictions (even indirectly) and, in any event, will incur onerous capital requirements if they continue to access third-country CCPs that have not been recognised – this would likely lead to such firms ceasing to access those third-country CCPs, resulting in a fragmentation in liquidity.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[Please provide data here]

ESMA's Steven Maijoor criticised the extremely rigid and burdensome process, and that equivalence decisions were taking much more time than expected.

Keynote Speech Steven Maijoor – Clearing the way towards an OTC derivatives union

http://www.esma.europa.eu/system/files/2015-1417_steven_maijoor_isda_europe_conference_speech_2015.pdf

ESMA – EMIR Review Report No 4 pp 19-21 – http://www.esma.europa.eu/system/files/esma-2015-1254_-_emir_review_report_no.4_on_other_issues.pdf

*Pp 20 – Para 105 - The process for the recognition of TC-CCP is extremely rigid and burdensome, as demonstrated by the limited number of recognition decisions taken so far. The equivalence decision process is* *taking much more time than expected. ESMA delivered its technical advice in September and October 2013 and as of today the equivalence determinations covered only a limited number of countries. Three years after the entry into force of EMIR, the majority of the TC-CCPs are still operating under a transitional regime. This puts at risk European clearing members and their subsidiaries clearing with these TC-CCPs and creates the potential for regulatory arbitrage between European and third country CCPs.*

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The EMIR Art 25 process needs to be more transparent and forthcoming and be granted in a timely manner.

FIA would like to make reference to a joint letter with ISDA to the European Commission (dated 15 December 2014) where we reiterated the importance of continued regulatory dialogue with foreign regulators outlining the impact in case the recognition of third country CCPs is not achieved in a timely manner.

## Example 2 for Issue 9 (Barriers to Entry)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**CRR – LEVERAGE RATIO**

**Please provide us with an executive/succinct summary of your example:**

EMIR and CRR IV do not mutually re-enforce the G20 objective of increasing the extent to which derivatives are cleared via CCPs. Whilst EMIR seeks to promote central clearing, the CRD IV-mandated regulatory capital costs and leverage ratio requirements applicable to central clearing have directly resulted in clearing brokers leaving the industry, thereby reducing access to central clearing. The feedback from our members is that this trend will continue. The key issue here is that the leverage ratio does not currently recognise the exposure-reducing effect of segregated margin: as a result, clearing members have much less balance sheet capacity to clear derivatives for their clients, which is actively hampering the successful implementation by the industry of the EMIR clearing obligation.

Considering the capital and resources required, it is now highly unlikely that new players will enter the market.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

FIA will be coordinating the submission of data to the Bank for International Settlements (BIS)in a future data collection exercise in response to the Basel Committee's Banking Supervision (BCBS) monitoring of the Basel rules (https://www.bis.org/bcbs/qis/). The data exercise is an official collection under the Basel Committee's Quantitative Impact Study (QIS) and is usually repeated semi-annually with end-December and end-June reporting dates. We believe this data will be able to evidence the impact of the leverage ratio on the provision of clearing services. We encourage the Commission to discuss the results of the data exercise with the BCBS.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The leverage ratio should be amended so as to recognise the exposure-reducing effect of segregated margin and that SA-CCR be adopted as a replacement for CEM in the leverage calculation, in order to address the shortcomings of the CEM model (as outlined in BCBS279). This is essential, to ensure that: there is sufficient balance-sheet capacity among clearing brokers to clear the derivatives that are declared subject to mandatory clearing under EMIR.

## Example 3 for Issue 9 (Barriers to Entry)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**EMIR and MIFIR Indirect Clearing provisions**

**Please provide us with an executive/succinct summary of your example:**

Indirect clearing under EMIR has not been successful for various reasons as outlined below:

On MiFIR indirect clearing provisions, kindly refer to our detailed response linked below:
https://fia.org/file/2885/download?token=oxG2XE1I9ow31BExxz_r_uTcgFvOsekUf1OLUSoMWZw

While we appreciate that ESMA has sought to address a number of the concerns raised by market participants in response to the previous consultation, in order to achieve a workable solution for the indirect clearing of ETD, whilst taking into account the requirements of Article 30 MiFIR, we believe that certain features of the current draft MiFIR RTS still pose significant legal and practical challenges, many of which the industry has been grappling with for some time in the context of indirect clearing of OTC derivatives under EMIR. If these challenges are not solved, this could result in a decline in market participants' willingness to engage in indirect clearing arrangements in light of the resultant operational, legal, re-papering, business, capital and compliance requirements.

Indirect clearing rules are intended to bring greater access to clearing for end-users and to reduce default risk for clients further down the chain. However, inappropriately designed and executed implementation could counter those aims. We are particularly concerned with the operational costs and complexities that would be introduced by the MiFIR RTS in their current form, as there is a risk that such costs and complexities may not be operationally supportable by all clearing members and their clients currently providing market access to indirect clients, which will reduce rather than increase accessibility to cleared derivatives markets for end-users. Such a decrease in accessibility would result in a less competitive market, with resultant increased costs for direct and indirect clients and concentration of systemic risk across a smaller number of entities.

The scale of the market upheaval – not least the requirement for clearing members and clients to repaper all indirect clearing arrangements at every level of the chain (i.e. many thousands of legal relationships) to accommodate the RTS (including structures which would be needed to meet the Article 5(8) obligations) – cannot be underestimated.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

On MiFIR indirect clearing provisions, kindly refer to our detailed response linked below:
https://fia.org/file/2885/download?token=oxG2XE1I9ow31BExxz_r_uTcgFvOsekUf1OLUSoMWZw

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

A number of FIA's concerns should be significantly ameliorated if the following key amendments are made:

- it should be clear that a clearing member may apply reasonable criteria (such as risk-based and/or commercial criteria) when deciding for which of its clients it is prepared to facilitate indirect clearing services;

- the application of the MiFIR RTS should be limited to clearing on an EU CCP of exchange traded derivatives entered into by an EU counterparty on an EU regulated market;

- each 'in-scope' entity in an indirect clearing arrangement should only be required to comply as far as practicable with its obligations under the MiFIR RTS (bearing in mind that there may be other entities in the chain that are not subject to MiFIR), should only have obligations in relation to the next person in the chain (subject to the porting or leapfrog requirements on clearing members) and should not be required to verify compliance with the RTS by other entities in the indirect clearing chain;

- clearing members should not be required to open more than one account of each type (i.e. NOSA/GOSA) at the CCP for holding the assets and positions of all of its indirect clients and similarly, other parties in the chain should not be obliged to maintain more than one account of each type (i.e. NOSA/GOSA) for indirect clients;

- requirements relating to porting should be removed or, if retained, they should be limited to GOSA structures and the "obligation of means" should be calibrated in such a way that it does not restrict the ability of clearing members to manage counterparty risk in the event of the default of a direct client; and

- requirements relating to Article 5(8) should be deleted, as they are not mandated by Level 1 and we strongly believe that these protections could be delivered through national or European legislation and may currently be available by choice through client asset regimes but that it is not feasible to outsource this task to individual entities in the chain of indirect clearing arrangements.

In addition, we are of the view that the requirements of the RTS should only apply to the first four parties in the clearing chain, to the extent that they are 'in scope' entities (and we note that a number of clarifications would be needed to address uncertainties in the RTS if this limitation is not adopted). We should also be grateful for guidance, possibly in the form of Q&A clarifying what is expected of clearing members in practice, in order to fulfil their "obligation of means" in respect of porting and leapfrog payments, if those requirements are not removed.

**Theme C. Interactions of individual rules, inconsistencies and gaps**

## Issue 10 – Links between individual rules and overall cumulative impact

Given the interconnections within the financial sector, it is important to understand whether the rules on banking, insurance, asset management and other areas are interacting as intended. Please identify and explain why interactions may give rise to unintended consequences that should be taken into account in the review process. Please provide an assessment of their cumulative impact. Please consider whether changes in the sectoral rules have affected the relevancy or effectiveness of the cross-sectoral rules (for example with regard to financial conglomerates). Please explain in what way and provide concrete examples.

## Example 1 for Issue 10 (links between individual rules and overall cumulative impact)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

DELINKING CRD IV FROM QCCP STATUS FROM EU AUTHORISATION UNDER EMIR

**Please provide us with an executive/succinct summary of your example:**

The application of Article 25 remains outstanding for a number of third country jurisdictions, including but not limited to the USA. The Commission's current efforts regarding the equivalence assessment of the legal and supervisory framework of third-country CCPs, which is a prerequisite for recognition of such CCPs by ESMA, is of vital importance for market participants. The combination of a lack of third-country CCP recognition and the expiry of the transitional provisions (on 15 June 2016) related to own funds requirements for exposures to CCPs in the Capital Requirements Regulation (CRR), could severely impact European firms (EU firms) acting on a cross-border basis from both a clearing and capital requirement perspective.

From a clearing perspective:

- OTC derivatives contracts subject to an EMIR clearing obligation: EU counterparties will be unable to clear these contracts through non-EU CCPs that have not been recognised under EMIR, even if clearing via a local clearing member, on the basis that an EMIR clearing mandate can be discharged only via an EU authorised CCP or a non-EU recognised CCP. This issue is exacerbated by the frontloading requirement to the extent that the clearing mandate starts phasing in prior to an official decision on the equivalence of the non EU jurisdiction, as continuing to clear on a CCP in a region without recognition may result in greater market disruption for those cleared trades have to be liquidated at the end of the frontloading window.
- OTC derivatives contracts not subject to that EMIR clearing obligation, which are voluntarily cleared: EU clearing members could not be direct clearing members of non-EU CCPs which have not been recognised under EMIR (Article 25 EMIR) Consequently, any clearing through such non-EU CCP

would only be possible (a) where the trades are not subject to an EMIR clearing mandate and (b) are cleared via a non-EU clearing member. For third country CCPs, there is a risk of open positions that have been voluntarily cleared on such third country CCP being "trapped" at that third country CCP with no possibility of closing them out: if such CCP has its application for EMIR recognition under Article 25 rejected, EMIR does not permit firms to enter into offsetting trades to close out the current portfolio. This results in the open positions being trapped at such third country CCP.

From a capital perspective: EU Banks and investment firms would not be able to continue to apply preferential capital treatment to CCPs not recognised by ESMA as these cannot be considered qualifying CCPs (QCCPs) under the CRR in the absence of a positive recognition decision. As a result, EU banks and investment firms will incur onerous and uneconomic capital requirements if they or their consolidated non-EU subsidiaries continue to access third-country CCPs that have not yet been recognised, or have simply failed to apply for recognition.

Such concerns are problematic not only for EU firms' continued access to third-country CCPs that have applied for recognition under EMIR, but also for EU firms' access to CCPs established in other third-country jurisdictions. Indeed, in addition to the jurisdictions where CCPs have applied for recognition, consideration should also be given when it comes to equivalence decisions for jurisdictions whose CCPs may not yet have applied for recognition but are adhering to the Committee on Payments and Market Infrastructures and International Organisation of Securities Commissions' (CPMI-IOSCO) Principles for Financial Market

Infrastructures (PFMIs). CCPs from these jurisdictions would have a strong incentive to apply for recognition where equivalence decisions are already in effect. Emerging markets represent important emerging markets with significant derivatives markets, particular for products such as FX and commodities and their own existing CCP infrastructure and European financial firms should be given the opportunity to participate in such markets without experiencing burdensome capital requirements which could place severe limitations on the amount of business transacted by EU firms in these jurisdictions, and in the worst case could force some firms to pull out altogether.

The current process for recognition seems to be largely driven by a third country CCP making an application.

We encourage the Commission to consider proactively engaging with CCPs in countries that have not made an application for recognition.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Please see comments made at example 1 for Issue 1 - Unnecessary regulatory constraints on financing-.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We consider that it is important to separate:

- the issues of recognition of a non-EU CCP under Article 25 as the basis for allowing counterparties subject to EMIR to satisfy their clearing obligation under EMIR by clearing through the non-EU CCP and for allowing non-EU CCPs to clear transactions on EU trading venues; and

- the issues of whether there are prudential reasons to restrict an EU firm being a clearing member of the non-EU CCP or whether the non-EU CCP should be treated as a QCCP for the purposes of the Capital Requirements Regulation.

**Example 2 for Issue 10 (links between individual rules and overall cumulative impact)**

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**INCONSISTENT GLOBAL TIMELINES**

**Please provide us with an executive/succinct summary of your example:**

Whilst the opportunity for a coordinated roll out of the G20 Commitments has now passed, there is still plenty of time and scope for a closer alignment of the European and US regimes. The EMIR review on which the European Commission has just commenced is the perfect opportunity for the EU and the US to align their standards, to promote international regulatory consistency and a level playing field, thereby mitigating the risks of arbitrage or business migration between the two regimes and promoting a fair competitive regime for all.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.) By way of example, note the issues as described in relation to the lack of equivalence determinations.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

The global key jurisdictions like the US and those in Asia must also be closely involved in such dialogue, as European business could as readily move east over time as west. Such loss of business would harm the creation of jobs and growth in Europe.

In order to better promote and facilitate the key regulatory tools of recognition and equivalence, more consistency in global regulation would be desirable.

To the extent possible and appropriate, we encourage harmonisation of product scope, types of entities to whom the regulation is subject and other key aspects of proposed regulation.

**Example 3 for Issue 10 (links between individual rules and overall cumulative impact)**

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**ACKNOWLEDGING THE IMPORTANCE OF THE MULTIPLE TRADING STRATEGIES AND DIVERSE CHARACTERISTICS OF PARTICIPANTS IN DERIVATIVES MARKETS**

**Please provide us with an executive/succinct summary of your example:**

There is an increasingly common undertone in recent EU and national Member State consultations that non-hedging related trading strategies are the scourge of financial markets, which leads to excessive volatility. Whilst this may be true in extremis, a degree of speculation in markets is necessary for them to function.

Different trading strategies of market participants promote price discovery, maintain accurately priced markets and can reduce market uncertainty and volatility. At the simplest level, market makers each provide a key service in ensuring the liquidity of financial markets, by matching buyers with seller. Pension funds rely on a degree of speculation in order to generate a reasonable rate of return for their members. If Europe is to experience an increase in jobs and growth, then speculation in derivatives markets has an important, necessary and healthy role to play, for wholesale industry markets and the real economy alike.

Such strategies play a key role in the chain of relationships between different market participants and to the end-user of all asset classes.

Despite their key role in the infrastructure, market makers and other liquidity providers have indicated their intention to leave certain markets, citing the imminent regulation (e.g. MiFID II / MiFIR) and associated increased cost of capital. This would lead to further unintended consequences of decreasing liquidity and concentration of systemic risk.

In general, MiFIR and CRD IV each envisage their future application to a wider range of firms than is the case today. In particular, MiFIR will reduce the availability of the “ancillary activities” exemption for users of commodities derivatives and CRD IV will apply to all non-bank entities engaged in commodity derivatives that are authorised as an investment firm under MiFID II once the current exemption for commodities dealers from Articles 493 and 498 of CRD IV expires at the end of 2017.

The primary focus of energy companies and commodity trading firms that may be required to register as an investment firm under MiFID II is not “how will we ensure we become compliant with MiFID II” but rather “how will my company deal with the fact that as a result of becoming an investment firm under MiFID II, the regulatory capital requirements under CRD IV will apply to me?”.

The additional capital costs that derive from application of CRD IV to such firms will result in significant increases in energy costs for end users and in the costs of raw materials for producers. This risks actively hampering the drive of the European Commission to promote jobs and growth within the European Union.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

In general, MiFIR and CRD IV each envisage their future application to a wider range of firms than is the case today. In particular, MiFIR will reduce the availability of the “ancillary activities” exemption for users of commodities derivatives and CRD IV will apply to all non-bank entities engaged in commodity derivatives that are authorised as an investment firm under MiFID II once the current exemption for commodities dealers from Articles 493 and 498 of CRD IV expires at the end of 2017.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We ask the European Commission to carefully consider the critical role that multiple trading strategies and diverse characteristics of participants in the derivatives market play.

**<u>Example 4 for Issue 10 (links between individual rules and overall cumulative impact)</u>**

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**EMIR – Article 4 Clearing Obligation – Frontloading**

**Please provide us with an executive/succinct summary of your example:**

Market participants are unable to accurately price trades that will be cleared at a future date. This will likely lead to a divergence in pricing and overall market disruption. This will likely hamper market liquidity during phase-in periods and may even disincentivise some market participants from hedging.

Whilst the analysis below refers to US CCPs, the concerns are equally applicable for all jurisdictions in respect of which an Article 25 recognition decision has yet to be made with respect to the CCPs in the applicable third country.

Category 1 and 2 counterparties entering into relevant transactions after the relevant frontloading date and clearing those transactions on US CCPs will not know whether they have to close out those transactions if the relevant recognition decisions are not in place by the start of the relevant frontloading period. This may have a detrimental effect on the willingness of market participants to continue trading and clearing on those CCPs and gives EU authorised CCPs an unwarranted form of competitive advantage in the interim (i.e. the certainty that the transaction can continue to be cleared on the CCP).

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

Given the challenges to date in reaching an EU-US agreement, market participants may remain concerned that the recognition will not be given in time and therefore may be reluctant to trade for clearing on US CCPs after the relevant frontloading date because of concerns that these issues will not all be resolved by the start date of the clearing obligation (and those Category 2 counterparties will need to put in place alternative clearing arrangements prior to the start of the window).

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

It is crucial to ensure that, going forward, the clearing obligation only applies to OTC derivatives contracts where those contracts are suitable for clearing, and that the mandates be implemented so as to minimize market disruption, ensure the continuity of markets participants' hedging programmes and to foster an environment where derivatives users are encouraged to reduce bilateral risk.

It would be helpful if the Commission and ESMA targeted achieving full recognition of all relevant third country CCPs before the effective date of a future clearing mandate.

**Example 5 for Issue 10 - Rules giving rise to unintended consequences**

**Position Limits – MiFID II**

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II).

**Please provide us with an executive/succinct summary of your example:**

Art 57 of MiFID II requires the establishment of position limits for commodity derivatives in EU markets. In the USA, position limits apply only to a small number of contracts and it appears increasingly unlikely that limits will be expanded to more contracts in the near future.

European position limits will need to be calibrated appropriately to ensure EU markets continue to function efficiently and effectively. The EU, being the only region to implement such widespread limits, will be at a competitive disadvantage to the USA or Asia if the position limits regime is too restrictive. In particular, commodity end-users (such as airlines or food producers) are concerned that the EU rules are so stringent that their application will lead to unintended consequences. There is no hedging exemption available for banks, meaning all contracts will fall under the position limits regime. Equally, the definition of economically equivalent contracts as proposed is so narrow that it does not allow effective netting of commodity contracts before position limits are applied. Once the limits are reached, banks will be unable to offer hedging services to their clients. In anticipation of the new regime, some banks have already exited the market and more may follow. The resulting gap may be filled by non-regulated participants located outside of the EU as well as non-EU trading venues that may offer look-alike contracts mirroring those available in the EU but without having to apply position limits. In consequence, liquidity (and thus jobs and growth) would be driven away from the EU.

Further, the aggregation rules proposed in the Level 2 to Art 57 of MiFID II will lead to the EU position limits regime having an extra-territorial effect as they require the aggregation of positions taken by subsidiaries or separate businesses operating within a group globally, leading to the aggregation of positions across independently managed businesses.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

MiFID II has not been implemented yet and the RTS on position limits has not yet been adopted. For more background, we refer to FIA's response to the MiFID II consultation.

We refer to remarks made by Christopher Giancarlo, CFTC Commissioner, on proposed US and EU position limits - "Imposing position limits now, whether it's under European rules or US rules, seems to me so out of time," Giancarlo tells Risk.net. "It's almost as if regulators are still proceeding with something when the whole world has moved against them, as if regulators are reacting to events present in the last decade, when commodity prices were rising and there was concern about excessive speculation in the market."

The CFTC's effort to impose position limits stems from a provision in the US Dodd-Frank Act, which was passed in July 2010, two years after a surge in prices for North Sea Brent and West Texas Intermediate (WTI) crude oil to levels above $147 per barrel.

It has to be noted that on December 21, front-month WTI futures on CME Group's Nymex exchange hit an intraday low of $33.98/bbl – a level not seen since February 2009 – while front-month Brent futures traded as low as $36.04/bbl [NB: the front-month Brent futures dropped even further in January 2016], their weakest since 2004.

Giancarlo further elaborates: "As restrictive and broad as the US position limits proposals are, the European ones are the US ones on steroids," Giancarlo says the US energy companies represented on his committee are much more worried about a lack of liquidity in commodity derivatives than the influence of speculation.

Alluding to one member's remark at an Eemac meeting in February 2014 that markets were suffering from "excessive hedging", rather than excessive speculation, Giancarlo says supporters of the position limits rule are trying to solve the wrong problem.

"Regulators are still furiously writing position limits rules to limit the role of speculators when the market is collapsing and the speculators are gone," he says. "My committee was more worried about excessive hedging because folks are worried about falling commodities prices and trying to hedge in an environment where the liquidity is moving away."

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Overly restrictive netting rules will impact end users ability to manage risk if as a result of restrictive position limits banks are unable to provide hedging services. This could be avoided by either introducing a hedging exemption for financial institutions or by at least widening the definition of economically equivalent OTC contracts. Further, the removal of the ability to net non-MiFID and MiFID instruments does not recognise fundamental market dynamics as MiFID instruments are frequently used to manage physical risk and are recognised as fungible for risk management purposes. Thus, netting of MiFID and non-MiFID instruments should be permitted. The extra-territorial effect could be avoided by aggregating only those positions held by EU entities.

## Issue 11 – Definitions

Different pieces of financial services legislation contain similar definitions, but the definitions sometimes vary (for example, the definition of SMEs). Please indicate specific areas of financial services legislation where further clarification and/or consistency of definitions would be beneficial.

## Example 1 for Issue 11 (Definitions)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**MiFID II**

**EMIR – definition of 'Derivative' and 'OTC Derivative'**

**Please provide us with an executive/succinct summary of your example:**

The definition of derivative links back to the list of financial instruments in MiFID. As a directive, MiFID has been implemented in different member states of the EU in different ways. One area where this has caused confusion is with respect to the boundary between FX spot and forward transactions, with the former being an unregulated product and the latter being a regulated product. Some member states have provided that any physically settling FX transaction would need to settle on a T+2 basis or less to be considered a spot transaction. However, the FCA has taken the position that transactions settling on a T+7 basis or less would not be "in scope" as being a regulated product. This means that certain transactions concluded in some member states would be regulated and subject to all of the risk mitigation requirements in EMIR as well as the reporting requirements but would not be subject to regulation in other member states.

This has been addressed to some extent by a Commission Delegated Act under MiFID II which (amongst other things) carves out transactions used to facilitate payment for goods, services or direct investment but with no further clarity on the types of transactions that would be covered.

**How to remedy**: A uniform application across all EU member states in applying rules and obligations is desirable.

**Example 2 Issue 11 – Definitions**

**Definition of Hedging for non-financial entities**

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

EMIR and MiFID II

**Please provide us with an executive/succinct summary of your example:**

In its EMIR Report No. 1, ESMA stated that "the classification of transactions as hedging or non-hedging would in most cases be left to non-financial counterparties with important limitations for their supervisors to verify compliance with the hedging definition, which is itself broad enough to raise interpretation issues". Yet, in the final draft MiFID II RTS on ancillary activities and on position limits, ESMA refers to the EMIR definition of hedging. Only transactions compliant with this definition may be deducted from the threshold calculations (for ancillary activities) or from the positions to which the limits apply (for position limits). This is inconsistent.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

Reference is made to ESMA's EMIR review report No.1
https://www.esma.europa.eu/sites/default/files/library/2015/11/esma-2015-1251_-_emir_review_report_no.1_on_non_financial_firms.pdf

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

If the hedging definition in EMIR was deemed unclear, the requirements, in particular those contained in the EMIR Q&As and requiring a direct link between a transaction and a hedge, should not be introduced in MiFID II.

**Example 3 Issue 11 – Definitions**

**CRDIV, CRR, MiFID II and EMIR**

**Please provide us with an executive/succinct summary of your example:**

There is a need for consistency between CRDIV, Capital Requirements Regulation (CRR), MiFID II etc. and EMIR. For example, CRR makes available certain preferential regulatory capital treatments for cleared trades, but the relevant provisions do not contemplate third country CCPs whose segregation requirements have been subject to positive equivalence assessments.

There is a need to ensure that definitions that are dependent upon determinations to be made in other legislation, e.g. equivalence, are clearly identified, tracked and assessed to minimise the impact of inconsistent application upon those subject to the legislation.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

Not only should defined terms in EMIR be aligned with terms used in other related legislation, but they would also ideally be aligned with the terms used by BIS and CPMI IOSCO. The application of certain sections of EMIR to particular counterparties (CCPs, clearing members, direct clients, indirect clients) and certain derivatives types is unclear.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

EMIR should further clarify to whom specific provisions apply, as regards EU / Non-EU CCPs, clearing members, direct clients, indirect clients etc., so as to avoid inconsistency of application and to ensure clear exemptions/default approaches where conflicts of law arise with third country legislation or non-relevance to the implementation of EU policy. EMIR should also clarify whether specific provisions apply to uncleared OTC derivatives and/or voluntarily cleared OTC derivatives and/or mandatorily cleared OTC derivatives and/or exchange traded derivatives.

## Issue 12 – Overlaps, duplications and inconsistencies

Please indicate specific areas of financial services legislation where there are overlapping, duplicative or inconsistent requirements.

### Example 1 for Issue 12 (Overlaps, duplications and inconsistencies)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**CREATING HARMONIOUS CROSS-BORDER REGULATION**

**Please provide us with an executive/succinct summary of your example:**

The European Commission continues to liaise with key global stakeholders from the legislative and regulatory community to further discuss and develop a process of creating regulation that is mutually reinforcing of their respective agreed agendas, is globally consistent and is harmonious. A roadmap for agreeing such process should be agreed in the short term. Equivalence determination processes should be clear, transparent and standardised.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.) As different jurisdictions have implemented various regulations at different times, a number of challenges for firms that clear in multiple countries can be observed.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Outstanding equivalence assessments under Articles 13 and 25 of EMIR, and Article 19(6) of MiFID must be expedited. Discussions with third country regulators should always commence as early as possible in the legislative process. The European Commission could increase its efficiency in pro-actively identifying and addressing conflicts of European laws with those of third countries and national Members States by establishing a dedicated team for this purpose

### Example 2 for Issue 12 (Overlaps, duplications and inconsistencies)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

**MiFID II / MiFIR – Reporting Obligations/ EMIR – Reporting Obligations**

Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency – **REMIT – Reporting Obligations**

Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on reporting and transparency of securities financing transactions and amending Regulation (EU) No 648/2012 – Securities Financing Transaction Regulations – **SFTR – Article 4 (Reporting Obligation)**

Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the

Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC – **Market Abuse Regulation (MAR) – Reporting Obligations**

**Please provide us with an executive/succinct summary of your example:**

Regulators have become increasingly reliant on the reporting of specific information in order to monitor market abuse, systemic risk and suspicious trading patterns – however, regulation has been implemented in an increasingly fragmented and piecemeal approach which has resulted in duplicative and complex reporting requirements, with firms submitting a number of different report to a number of trade repositories (whether commercial enterprises or 'public utility'). Simultaneously, regulators struggle to collate data, collecting the wrong data, or using data collected for a purpose other than what it was meant for. Moreover, constant fine-tuning and tweaking to existing systems, and multiple workstreams dealing with a number of different regulations, results in disproportionate costs for firms.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

[provide data here] Reference is made to the duplicative and complex reporting requirements and issues observed and widely reported under i.e. EMIR.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

A holistic view of reporting should be taken, with regulators consolidating the reporting requirements into a single regulation. This should aim at streamlining and simplifying existing burdens, and regulators should also seek to give granular levels of guidance on the data they expect to receive.

## <u>Example 3 – Issue 12 – Overlaps, duplications and inconsistencies</u>

### Position reporting obligations under MiFID II

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II).

**Please provide us with an executive/succinct summary of your example:**

Article 58 of MiFID II prescribes the position reporting of commodity derivatives positions by (a) investment firms to regulators for OTC commodity derivatives transactions (article 58.2), (b) participants of regulated markets (RMs) and MTFs, and (c) clients of OTFs to the market operator for exchange traded commodity derivatives (article 58.3). This reporting shall include positions taken on own account as well as "*those of their clients and the client of those clients until the end client is reached*".

It will be extremely challenging if not impossible for market participants to comply with the obligations in Art. 58 (2) and (3), as investment firms and participants are not able to determine when the end of the client chain has been reached. They only have relationships with their own clients. Passing on of client data without consent is breaching data protection laws in the EU. Clients of other intermediaries in the transaction chain would have to waive their data protection to enable the financial intermediaries to comply with the reporting obligation. Such disclosures may be legally challengeable in a number of jurisdictions, especially those where criminal sanctions are attached to breaches of data protection or where the end-client is located outside of the EU. In addition, disclosure of such information is commercially highly sensitive for many end-clients, in particular investment fund managers.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

MiFID II/MiFIR has not yet been implemented but there were similar issues under Dodd Frank in the US, i.e. conflicts between obligations to disclose and privacy laws.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We believe there are three possible remedies to avoid the above conflict between the position reporting end-client requirement in Art. 58 (2), (3) and European and national data protection laws:

1) Remove the investment firm/ participant end-client reporting requirement as currently set out in Art 58 (2) and (3) of MiFID II and replace it with an obligation on the end-client to report; or
2) Introduce a best efforts obligation in Art. 58 (2) and (3) of MiFID II to reflect the fact that due to privacy laws and commercial sensitivities investment firms will struggle to obtain information about the positions of its clients' clients; or
3) Waive the application of privacy laws.

## Example 4 – Issue 12 – Overlaps, duplications and inconsistencies

### MiFID II – Third Country firms engaged in dealing exclusively on own account or providing services/performing investment activities outside the EU to clients outside the EU when accessing European Markets through Direct membership or DEA

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II).

**Please provide us with an executive/succinct summary of your example:**

The status of third country firms remains an area of substantial uncertainty under MiFID II. In particular third country firms engaged in either dealing exclusively on own account or providing services/performing activities outside the EU to clients outside the EU when accessing EU trading venues through direct membership / participation or through direct electronic access (DEA) arrangements.

Various scope provisions under Articles 1(1) and 1(2) of MiFID II and Article 1 of MiFIR refer separately to investment firms and third country firms providing investment services or performing investment activities through the establishment of a branch in the EU lend to the analysis that a third-country firm is a different legal concept to an investment firm. Thus provisions which affect investment firms without specific reference to third-country firms do not by definition apply to third-country firms.

Third country firms likewise would not fall under the authorisation requirement as they do not have a home Member State in terms of article 5(1) of MiFID II.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

**[PROVIDE EXAMPLE]**

Two aspects of third country firm provisions of services in the EU are expressly addressed in MiFID II / MiFIR but neither would apply where the third country firm is solely providing services or performing investment activities outside the EU to clients outside the EU or is engaged in dealing exclusively on own account.

With regard to supervision, overseas firms that are direct members of EU trading venues would be subject to the same organisational requirements as EU investment firms because trading venues' obligations under MiFID II will require them to ensure that all members meet the same level of systems and controls. Likewise for those third country firms accessing EU markets indirectly, DEA providers will serve as a gateway, ensuring clients' compliance with EU standards and safeguarding a level playing field.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We support the view that member states retain their discretion on how to implement MiFID II, particularly the UK's proposal to retain its existing regime going forward which would preserve the ability of third country firms engaged in either dealing exclusively on own account or providing services/performing activities outside the EU to clients outside the EU, and that access EU trading venues through direct electronic access arrangements, to continue to do so without establishment and authorisation of a branch or registration with ESMA.

## Issue 13 – Gaps

While the recently adopted financial legislation has addressed the most pressing issues identified following the financial crisis, it is also important to consider whether they are any significant regulatory gaps. Please indicate to what extent the existing rules have met their objectives and identify any remaining gaps that should be addressed.

## Example 1 for Issue 13 (Gaps)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**SUSPENSION OF THE CLEARING OBLIGATION UNDER EMIR**

**Please provide us with an executive/succinct summary of your example:**

Under EMIR, the clearing obligation cannot be terminated or suspended as a matter of urgency in extreme circumstances. This means that CCPs may find themselves clearing more risk in a contract or product than there would be market capacity to manage upon a member default.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Reference is made to pp 8 Para 33 ESMA's own recommendation to the EMIR Review

http://www.esma.europa.eu/system/files/esma-2015-1254_-_emir_review_report_no.4_on_other_issues.pdf

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

In line with ESMA, we recognise that there is a gap with regard to the possibility of regulators to suspend the clearing obligation – ESMA recognises the lack of possibility to suspend the clearing obligation in situations of extreme market distress as the most problematic issue related to the EMIR text.

## Example 2 for Issue 13 (Gaps)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**EMIR – CCP Clearing Services/CCPs should offer legally segregated, limited resources clearing services**

**Please provide us with an executive/succinct summary of your example:**

Many CCPs currently allow contributions under default waterfalls to be available to satisfy shortfalls in capital arising from defaults across different product clearing offerings. This means that client and clearing member assets may be used to satisfy shortfalls in capital arising from defaults in services which they potentially may not even use.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Without limited recourse, the CCP resolution process would become more complex as a default in one clearing service could bring down all of a CCP's clearing services, which would lead to less resilient CCPs and possible contagion across the financial system.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

EMIR should be amended to require CCPs to offer legally separate, segmented and limited recourse clearing services for each asset class or other class of instruments or liquidation group to reduce contagion risk.

EMIR should require that CCPs that offer multiple clearing services establish separate default funds for each service, with no recourse to the default funds of the other limited recourse clearing services.

EMIR should also prevent CCPs from being able to borrow from or use the non-depleted pre-funded resources available in other limited resource services under resolution.

## Example 3 for Issue 13 (Gaps)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**EMIR Article 28 – CCP Risk Committees**

**Please provide us with an executive/succinct summary of your example:**

EMIR provisions on the membership structure, role, and powers of CCP risk committees are not granular enough. CCP risk committees provide checks and balances on the commercial impetus of the CCP, ensuring that risk management is central to a CCP's processes. CCP rules should underline the importance and continuity of the function such that granular standards on membership are established.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

Given the systemic nature of CCPs and the commercial incentives resulting from the clearing mandate, CCP Risk Committees provide a critical "check and balance" to ensure risk management is at the heart of a CCP's activities.  Robust, granular standards on membership and the role of powers of a CCP Risk Committee ensures it can continue to perform this function.

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

EMIR should be amend to require that CCPs incorporate the following risk governance practices:

- Explicit members (risk / trading / operational) and seniority / experience requirements;
- Allowance of risk committee members to seek internal expertise on material risk matters i.e. waiver of confidentiality for non-commercial matters.

## Issue 15 – Procyclicality

EU rules have been put in place to make the financial system less procyclical and more stable through the business and credit cycle. Please indicate whether some rules have unintentionally increased the procyclicality of the financial system and how.

### Example 1 for Issue 15 (Procyclicality)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**EMIR –ARTICLE 28 OF RTS 153/2013**

**Please provide us with an executive/succinct summary of your example:**

In providing only 3 prospective alternative means to limit margin procyclicality for a variety of contract types, Art 28 of RTS 153/2013 does not take into account the myriad of account asset class nuances that, for instance, offer a means that sensibly limits margin procyclicality for seasonal energy contracts

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)n/a

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

Alternative means to limit procyclicality for a variety of contract types should be provided.

### Example 2 for Issue 15 (Procyclicality)

**To which Directive(s) and/or Regulation(s) do you refer in your example?**

(If applicable, mention also the articles referred to in your example)

**LACK OF INTERNATIONAL USE OF ANTI PRO-CYCLYCALITY BUFFER**

**Please provide us with an executive/succinct summary of your example:**

No jurisdiction other than Europe appears to consider procyclicality as explicitly as EMIR, which often leads to differences in margining for equivalent contracts in different jurisdictions.

**Please provide us with supporting relevant and verifiable empirical evidence for your example:**

(please give references to concrete examples, reports, literature references, data, etc.)

n/a

**If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We ask the Commission to provide more clarity on how it has addressed and proposes to address the lack of procyclicality in third country legislation in the context of equivalence assessments pursuant to Article 25 of EMIR.