Position of DAI, BDI and VDT on the ESMA's Disussion Paper "Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories"

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Deutsches Aktieninstitut (DAI)[1], Bundesverband der Deutschen Industrie (BDI)[2] and Verband deutscher Treasurer (VDT)[3] welcome the opportunity to comment on the ESMA discussion paper on "Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories". Our answers to the questionnaire represent the view of non-financial companies using derivatives almost exclusively to hedge against risks accruing from their commercial or treasury activities.

Our remarks focus on chapter „OTC derivatives" of the discussion paper and especially on the criteria determining derivatives used for "reducing risks directly related to the commercial acitivity or treasury financing activity" as defined in EMIR (in the following "hedging") and the definition of the clearing threshold. ESMA should unambiguously clarify that hedging is acknowledged as risk mitigating without referring to hedge accounting pursuant to IFRS or other national accounting rules. Otherwise the vast majority of non-financials which do not apply these accounting standards, especially for reasons of complexity and lacking feasibility, could not benefit from the clearing exemption. Furthermore, the list of risks which determine whether a derivative qualifies as hedging instrument has to be complete. In addition, the company's auditor should play a pivotal role in the enforcement process.

Also of great importance for non-financial companies is the definition of the clearing threshold. The calculation of the clearing threshold should reflect adequately the systemic relevance of the company's risk position. For this reason an economically appropriate measure should be chosen in determining the risk position. Furthermore, collateral already posted and netting agreements should be fully taken into account as well. We also call for a group level threshold in relative terms which takes into account the size of the non-financial counterparty.

ESMA should also consider the specifics of non-financial companies as regards the risk management and reporting requirements. E.g. the obligation for a frequent portfolio compression is not in any case reasonably appropriate for derivatives held for hedging purposes. Furthermore, we call for a proportionate reporting regime for derivatives of non-financial companies. ESMA should take into account that the application of the proposed reporting regime would burden especially mid-sized companies without any benefit from a supervisory perspective. Therefore, ESMA should allow

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1 Deutsches Aktieninstitut e.V. (DAI, www.dai.de) is the association of German exchange-listed stock corporations and other companies and institutions which are engaged in the capital markets development.

2 Bundesverband der Deutschen Industrie e.V. (BDI, www.bdi.eu) is the umbrella organisation of German industry and industry-related service providers. It represents 38 industrial sector federations and has 15 regional offices in the German Länder. BDI speaks for more than 100,000 private enterprises – 98 % small and medium sized – employing around 8 million people. Membership is voluntary.

3 Verband Deutscher Treasurer e.V. (VDT, www.vdtev.de) is the official German association of Corporate Treasurers representing more than 950 treasury professionals from 450 companies.

non-financial companies to delegate the respective reporting to the financial counterparty without restrictions. Reporting of group transactions which are used for hedging purposes should strictly follow the language provided by EMIR.

From a non-financial perspective the requirements regarding bank guarantees as an alternative to cash for centrally cleared derivatives are also crucial. The strict requirements proposed by ESMA will contradict the aim to provide non-financial companies with the possibility to post bank guarantees instead of cash collateral which would increase non-financial companies' costs of central clearing disproportionally.

Please find below our answers to the questions. We would appreciate if you could take our proposals seriously into account.

OTC Derivatives

Q1: In your views, how should ESMA specify contracts that are considered to have a direct, substantial and foreseeable effect within the EU?

It is extremely difficult to define transactions of third country counterparties which might have the above mentioned effects within the EU. Taking this into consideration it is rather impossible to reach legal certainty in specifying the respective contracts. Furthermore, it is far from being clear how this provision could be appropriately enforced in cases in which both counterparties are residing outside the EU where ESMA or the competent national supervisory authorities are not allowed to execute their competences.

Q2: In your views, how should ESMA specify cases where it is necessary or appropriate to prevent the evasion of any provision of EMIR for contracts entered into between counterparties located in a third country?

Subsidiaries of non-financial counterparties especially established in emerging markets (e.g. China, India and Russia) contract with banks that are domiciled in these countries as well. The reasons for these business relations with third-country banks instead of using intra-group transactions are inter alia legal barriers for the cross border flow of capital imposed by the respective government or restrictions to convert the domestic currency into Euro. Evading the provisions of EMIR is no reason for non-financial companies to execute these transactions at all. ESMA should acknowledge this matter of fact when specifying the above mentioned cases.

Furthermore, to avoid duplicate or conflicting rules Art. 9a EMIR grants the EU-Commission the power to enact implementing acts which would declare third-country rules as equivalent to EMIR. The third-country provision should not conflict with these implementing acts. It should be ensured that counterparties domiciled in third-countries for which a respective implementing act affirms equivalence with EMIR should be outside the scope of Art. 3 para. 1 lit a (v) EMIR, as these counterparties already have to comply with a regulation similar to the EMIR rules.

Q3: In your views, what should be the characteristics of these indirect contractual arrangements?

We believe that being a client of a general clearing member should be sufficient to be considered an 'indirect contractual arrangement' and therefore to assess compliance with the clearing obligation. Additionally arrangements to clear deals with central counterparties after conclusion OTC should be considered as contractual arrangements sufficient to meet the clearing obligation triggered by EMIR.

Q4: What are your views on the required information? Do you have specific recommendations of specific information useful for any of the criteria? Would you recommend considering other information?

The information required in the notification process should not indirectly promote the standardisation of contract features. It should be ensured that the flexibility to choose the most suitable contract terms (e.g. besides ISDA Master Agreements) is remained.

Q5: For a reasonable assessment by ESMA on the basis of the information provided in the notification, what period of time should historical data cover?

The time period should at least cover 12 months. Short-term liquidity can differ significantly in financial markets.

Q6: What are your views on the review process following a negative assessment?

To ensure legal certainty it is important that market participants can rely on a modus operandi for a reasonable time period. We suggest holding such a status for at least 12 months.

Q7: What are your views regarding the specifications for assessing standardisation, volume and liquidity, availability of pricing information?

It is important that the highest possible degree of flexibility is retained for those derivatives that non-financial companies require for their hedging operations. It should also be noted that these derivatives are acknowledged to be not of systemic relevance. Therefore, more individualized structures should not be moved to CCPs. We suggest reviewing the data on standardization (e.g. percentage of standard tenors traded versus bespoke ones), liquidity, and trading frequency. These issues indicate the degree of involvement of tailor-made structures, which will often have a hedging background. It is also important to evaluate how many traders are providing the liquidity in an instrument, as in times of market stress a low number of market makers may not be able to assure it. We also suggest developing a user typology as a criterion: it would be of interest what percentage of the volume is done by banks and other traders in financial markets, and what is due to non-trading (non-financial) counterparties. The latter would presumably have a hedging background, and should therefore not be obliged to be centrally cleared.

Q10: In your view, does the above definition appropriately capture the derivative contracts that are objectively measurable as reducing risk directly related to the commercial or treasury financing activity?

We welcome that ESMA accepts alternatives to hedge accounting for the definition of hedging transactions in the meaning of derivative contracts, which qualify to mitigate risks directly related to the commercial activity or treasury finance activity. This is suitable against the background that many German companies (and surely other European companies as well), especially small and mid sized corporates, do not apply these accounting standards. One reason for not applying these standards is the complexity which would burden many companies disproportionally. Another is the fact that hedge accounting rules are lacking the flexibility to meet the specifics of many derivative contracts.

The results of a survey conducted by VDT and DAI among 205 corporates in 2011 show evidence for this assumption: Only 17 per cent of companies with an annual turnover of less than 100 million Euros apply the respective IFRS or national accounting rules for their entire derivative exposure. Even in bigger companies the situation differs not very much: Only 26 per cent of the companies with an annual turnover of more than 100 million Euros apply the respective IFRS or national accounting rules.

Nevertheless, we do not understand why ESMA makes “reference to European accounting rules” regarding the risks mentioned in no. 29 of the discussion paper. To avoid misunderstandings ESMA should unambiguously clarify that “hedging” is recognized as risk mitigating irrespective of the application of any hedge accounting rule (neither IFRS nor the creation of e.g. *“Bewertungseinheiten”* which are allowed under the German commercial code).

Furthermore, the following aspects should be reflected in the final technical standards:

1) All risks should be considered (no. 29)

The list mentioned in no. 29 should cover all relevant risks stemming from the commercial and treasury activities mitigated by non-financials through derivatives:

- Derivative instruments used to mitigate risks related to corporate actions, e.g. capital decreases or increases, share buybacks, convertible bonds and employee stock ownership plans, are not yet considered. These corporate actions are a part of the treasury activity and should be accepted as risk mitigating under EMIR.

- We are wondering if the term “changes in the value off…” also include the changes of the cash flows. As both asset values and cash flows are hedged by derivatives this should be clarified.

Furthermore, the interplay between lit. a and lit. b is hard to understand. While lit. a inter alia considers the potential change in the value of commodities, lit. b does not explicitly refer to fluctuations in commodity prices. For reasons of clarity fluctuations in commodity prices should be added to lit. b as well. This would also be in line with recital 16a EMIR which states that the definition of risk mitigating derivatives should consider “fluctuations in interest, foreign exchange, inflation rates or ***commodity prices***“. Furthermore, although lit. a explicitly refers to the anticipated exposure, lit. b does not. The provision that reasonably anticipated value changes are acknowledged as risk mitigating should therefore be inserted in lit. b as well. We also miss under lit. b the risk that the business partner defaults before the outstanding obligation (especially trade receivables) is settled. Some non-financial companies hedge this kind of risk with credit default swaps. Mitigating the credit risk stemming from trade finance assets is closely linked to the commercial activity because the focus is clearly on commercial transactions. Thus, credit risk should be included in the list.

2) National accounting standards should also be acknowledged (no. 39)

As mentioned above hedging pursuant to existing accounting rules should be an option and not an obligation. In any case, the hedging definition in no. 30 should not exclusively refer to hedge accounting according to IFRS but also to national hedge accounting rules, as far as they are applied by the companies.

3) Other issues not yet mentioned

We understand that ESMA's proposal reflects preliminary thoughts and does not outline the final approach how the EMIR-exemption for non-financial companies will be implemented. As a contribution to the ongoing process, we would like to add some further issues not yet mentioned in the discussion paper:

a) ESMA should be aware that risk mitigation strategies need not to cover the whole underlying business. Based on a cost-benefit-analysis it is common practice to hedge only a part of the operative business. Furthermore, ESMA should also include common used risk management practices like macro, portfolio or proxy hedges in the technical standard, which are also “economically appropriate for the reduction of risks” as stated in recital 16a EMIR. By applying these practices it is impossible to directly allocate one derivative to one respective underlying business.

b) ESMA should also acknowledge the role of the company’s auditor monitoring the prudent application of the hedging definition. This would also help to keep the enforcement process as lean as possible – for the benefit of supervisory authorities, corporates and their stakeholders. To examine which derivatives are applied by non-financial companies to mitigate commercial or treasury risks should be part of the annual audit (e.g. as negative statement). Reference could also be made to the overall risk management strategy of the non-financial counterparty which would also reflect the requirement laid down in recital 16a EMIR ([…] „due account should be taken of that non-financial counterparty’s overall hedging and risk mitigation strategy“.) For instance, German companies are already obliged by the national commercial code to disclose details of their risk management strategy including methods to mitigate risks stemming from their business activities. The compliance with this transparency rules is certificated by the auditor.

Q11: In your views, do the above considerations allow an appropriate setting of the clearing threshold or should other criteria be considered? In particular, do you agree that the broad definition of the activity directly reducing commercial risks or treasury financing activity balances a clearing threshold set at a low level?

We do not agree with the approach of ESMA to set the clearing threshold at a low level. Instead, the level of the clearing threshold should reflect Art. 7 para. 4 lit. a EMIR which states that the value of the threshold should take into consideration the "systemic relevance" of the derivative exposure. Furthermore, certain hedges may not fall under the final definition of hedging even if they are risk-mitigating from an economic point of view. This may happen e.g. due to enforcement practices or legal uncertainties, so that for reasons of flexibility an appropriate buffer is justified before the clearing threshold is finally crossed.

In addition, to provide coherence with other regulations implemented in non-EU countries and to avoid disruptions in the cross-border-flow of capital ESMA should duly take into account already existing rules concerning derivatives, especially those incorporated in the US-Dodd-Frank-Act. According to this, the rule proposed by the US Commodity Futures Trading Commission (CFTC)[4] also provides a good guidance how to define the exposure mark-to-market value which is deemed as risk relevant: USD 3 billion for "rate swaps" and USD 1 billion for other derivatives.

Furthermore, we wish to add some comments on the approach proposed by ESMA defining the clearing threshold:

1) Valuation of the derivatives: In fact the notional value, which is proposed by ESMA to calculate the „speculative" derivative exposure, is easy to be applied. Nevertheless, the notional value is not appropriate to measure the economic value of a derivative instrument for the following reasons:

- The notional value does not properly take into account that the derivative instrument can be in, at or out of the money. On portfolio level the different economic values of the derivatives are compensating each other to a certain extent. Therefore, the approach to calculate derivatives by notional value would substantially inflate the derivative exposure and would not reflect adequately the portfolio risk of the non-financial counterparty.

- As the derivatives in question are for "speculative" purposes an adequate risk management process should be in place to manage the incorporated risk appropriately. An important element of the risk management should be the implementation of risk sensitive pricing methods as for instance Art. 8 para 1a calls for. Therefore, a counterparty which invests in "speculative" derivatives should in general be able to manage and to measure its exposure beyond the notional value.

Instead of referring to the notional value ESMA should rather focus on the ***negative*** market value of the uncollateralised derivative exposure only, which adequately reflects the current downside credit risk of the non-financial counterparty. Reference to the negative market value is important, as only in this case the non-financial com-

4 See http://www.cftc.gov/LawRegulation/FederalRegister/ProposedRules/2010-31130.

pany has an obligation vis-à-vis its counterparty and could therefore theoretically pose a risk to that counterparty. Referring to market values would also ensure that coherence with the CFTC-rule is achieved: The threshold for being acknowledged as "Major Swap Participant" refers inter alia to the "uncollateralized mark-to-market exposure".

2) Pay due attention to approved risk mitigation techniques: To be consistent with recital 16b EMIR risk mitigation techniques already applied by the non-financial counterparties should be considered in the calculation of the clearing threshold ("[…] recognise the methods of risk mitigation used by non-financial counterparties"). Therefore, the derivative exposure relevant for the calculation of the clearing threshold should be adjusted by bilateral netting agreements and collateral already posted. To incorporate netting agreements would comply with art. 7 para. 4 lit. a EMIR which states that the value of the thresholds "shall be determined taking into account […] the sum of ***net positions and exposures*** by counterparty […]". Taking into account netting agreements and collateral is also a general approach pursued in other regulations, for instance in the capital requirements for financial institutions. Specifically, secured derivatives should be excluded from the calculation of the clearing threshold. This would be coherent with the CFTC's proposal which refers in its definition of "Major Swap Participants" to the "***uncollateralized*** mark-to-market exposure".

3) Threshold at group or at legal entity level?: ESMA discusses whether the threshold should be calculated at group level or at the level of every legal entity of the group. We understand that ESMA favours the group level option which we also strongly support. Firstly, this approach would be in accordance with art. 7 para. 3 EMIR which states that the calculation of the clearing threshold should „include all the OTC derivative contracts entered into by the counterparty or by other non financial entities within the group to which the non financial counterparty belongs". Secondly, referring to the group level would also appropriately reflect that non-financial companies often centralise their risk management through e.g. a financial subsidiary which manages risks on account of other group entities. The derivative exposure of the whole group is, thus, concentrated on the level of the financing subsidiary or at the headquarter level. The threshold should therefore refer to the group exposure.

4) Proportional or absolute threshold?: In defining the threshold due attention should be paid to the fact that non-financial companies using derivatives differ in size due to the business model of the non-financial company. The size of a company is also crucial for its ability to absorb risks. On the one hand, this should be reflected by a ***proportional*** threshold which takes into account e.g. the balance sheet total, the total annual turnover or the aggregate derivative exposure of the whole group. On the other hand, a ***de minimis activity*** defined as a threshold in absolute terms, which is also proposed by the CFTC, should avoid the burden of computing the relative threshold especially for small and mid sized non-financial companies.

5) Threshold for the whole portfolio or for different asset classes: A threshold taking into consideration the whole portfolio would be easy to apply and to monitor. Nevertheless, in some cases a higher threshold could be economically justified to cover the specifics of certain derivatives adequately. For instance, the CFTC has developed a threshold for "rate swaps" which is three times the general threshold.

Q12: What are your views regarding the timing for the confirmation and the differentiating criteria? Is a transaction that is electronically executed, electronically processed or electronically confirmed generally able to be confirmed more quickly than one that is not?

Although we agree that a timely trade confirmation of both counterparties is important to ensure legal certainty that the transaction has become effective we doubt that a separate confirmation process is needed in any case. Banks regularly record the conversation with the respective client electronically when derivative contracts are agreed bilaterally on the phone. These records can be used when the counterparties differ in their opinion as regards the terms of the transaction. For these cases, a separate confirmation process would be superfluous.

While non-financial companies are in many cases able to confirm their trades quickly, the length of the confirmation process depends on the specifics of the transaction. Regarding some risk-mitigating derivatives, which are in general customized and therefore base on much more “individual” contract specifics, the confirmation process takes more time compared to more standardised products. It is important to note that a non-financial company that has crossed the clearing threshold will still need to do tailor-made hedging transactions as before. Therefore the timing requirements should not be linked to the threshold, but to the nature of the counterparty and the respective transaction. The latter should refer to the hedging definition, as non-hedging transactions are likely to be very standardized trading instruments, which can be reported in a shorter timeframe. Therefore, transactions which are not separately recorded and which are used for risk mitigating purposes should be confirmed by non-financial counterparties ***four business days*** after the execution, others in ***two days***.

Nevertheless, ESMA should also take into consideration that the confirmation of more complex transactions cannot be processed in the above mentioned time period [e.g. ‘long confirmations’; additional (not prior mentioned) legal terms included in the confirmation; involvement of different departments within a company]. For these transactions the confirmation will take 5 to 10 business days without becoming undue. ESMA should therefore acknowledge a preliminary confirmation regarding the economic terms, which is often exchanged by the counterparties in order to value the derivative, as equivalent to the “full” confirmation.

In summary it is very important to acknowledge the wide spectrum of derivative transactions with different practices in the way and time legs they are confirmed. Some of the transactions can be confirmed very quickly others require several business days. Insofar establishing a confirmation concept with fixed time limits ignoring the specifics of transactions is not really convincing. This holds particularly true in view of no. 41 of the discussion paper. We doubt the appropriateness of modifying existing practices without a sound justification. Existing practices reflect well proved processes developed over years. There is always a rational behind existing practices, which should not be ignored. Legal disputes have never been a relevant problem in derivative markets, one reason for this is that the legal framework has been developed and standardized over decades now. This should not be jeopardized by non-viable confirmation deadlines.

Q13: What period of time should we consider for reporting unconfirmed OTC derivatives to the competent authorities?

As confirmation is usually possible within four business days after the execution (if preliminary conformations for complex transactions are recognized as suggested above) reporting of unconfirmed derivative contracts should take place after five business days.

Q15: Do you think additional criteria for marking-to-model should be added?

ESMA should take into consideration that it is possible to reasonably assign market values to a derivative instrument even in the case of illiquidity. An illiquid instrument can be appropriately valued if the value drivers of the derivative in question (for instance spot market prices or volatilities) are sufficiently liquid. Furthermore, to require a board approval as laid down in criterion 45e (p.13) is not justified. Such risk models will in practice be calibrated at lower levels.

Q16: What are your views regarding the frequency of the reconciliation? What should be the size of the portfolio for each reconciliation frequency?

Considering the number of derivatives is not appropriate to determine the frequency of portfolio reconciliation as this does not reflect the risk of the derivative exposure adequately.

To reconcile portfolios held with 10 or 15 banks even on a quarterly basis would bind capacities especially of small and mid-sized non-financial companies disproportionally. A permanent reconciliation process is also not necessary when the confirmation process is adequately implemented (see our answer to question 12). Therefore, for non-financial companies which have not exceeded the clearing threshold the portfolio reconciliation should be performed once a year by the company's auditor as part of the annual audit. This would be in line with the requirement in Art. 8 para. 1 lit. b EMIR which states that the formalised process in order to reconcile portfolios should be "robust, resilient and ***auditable***".

Q17: What are your views regarding the threshold to mandate portfolio compression and the frequency for performing portfolio compression?

Derivatives used by non-financial counterparties for hedging purposes are in general held until maturity or will be bilaterally adjusted in case the underlying business or market expectations have changed. As long as there is an underlying business, there is no reason for a portfolio compression which is processed to eliminate redundant contracts simply because there are no such contracts.

Against this background ESMA should not make a portfolio compression mandatory for non-financials which use derivatives almost exclusively for hedging purposes. This would be in line with EMIR which does not explicitly call for a portfolio compression.

Q18: What are your views regarding the procedure counterparties shall have in place for resolving disputes?

The existing market infrastructure and practice are sufficient to manage disputes. Therefore, non-financial companies do not have many difficulties with the management of disputes. Firstly, disputes are relatively rare phenomena. Secondly, they are resolved relatively smoothly, e.g. by providing evidence with existing records of phone calls. Therefore, we think it is justified to keep the process to resolve disputes for non-financials quite lean.

Q19: Do you consider that legal settlement, third party arbitration and/or a market polling mechanism are sufficient to manage disputes?

Yes, from a legal perspective OTC derivates are normal contracts which are perfectly covered by existing civil law in view of legal content and by civil jurisdiction from the enforcement perspective. Insofar any change to the existing set up is more likely to raise new problems rather than providing a solution. It is important to acknowledge that the market has developed a reliable set of standard documentations to transact derivatives. This documentation is fully in line with civil and – more important – European bankruptcy regulation.

Q20: What are your views regarding the thresholds to report a dispute to the competent authority?

The overall goal of EMIR is to address issues of systemic relevance. This principle should also give the guidance for the thresholds to be defined in view of this reporting obligation. Only disputes of systemic relevance should be reported to the competent authorities.

Q21: In your views, what are the details of the intragroup transactions that should be included in the notifications to the competent authority?

It is very likely that all non-financial companies exceeding the clearing threshold will apply for the group exemption. Therefore, we expect a vast number of notifications which will take time for the supervisory authorities to be thoroughly analysed. For reasons of legal certainty it is very important that ESMA clarifies that intragroup transactions are not obliged to be bilaterally collateralised until the notification process is finalised. Otherwise this would lead to the paradox situation that an intra-group transaction has to be collateralised until the exemption becomes valid.

In order not to overstretch scarce capacities especially of non-financial companies, which have not yet implemented the required reporting structures, the notification process should be kept as lean as possible. In our view it would be sufficient, that the company aggregates its intragroup transactions per asset class and reports the aggregated volume to the competent authority.

Regarding the issue “practical and legal impediments for the prompt transfer of own funds” we think that ESMA should consider the legal specifics in the respective jurisdiction where the group entities are domiciled (e.g. whether there are legal barriers hindering the flow of capital). The respective counterparty should confirm that there are no such impediments to its best knowledge (otherwise group transactions would not take place anyway).

Q22: In your views what details of the intragroup transactions should be included in the information to be publicly disclosed by counterparty of exempted intragroup transactions?

Intragroup transactions do not constitute counterparty risk towards third parties, but information on intragroup transactions is of particular confidentiality because the risk allocation strategy can be revealed by improper disclosure. In order to limit the potential damage we believe that no additional trading data should be publicly disclosed for groups compared to individual companies. If any trading data has to be published it must be ensured for reasons of confidentiality that the figures of intra-group transactions disclosed shall not allow competitors to gain insights on hedged exposures of subsidiaries. Therefore, figures potentially to be disclosed by the counterparty should present an appropriate level of aggregation. We suggest following the example of the Depository Trust & Clearing Corporation (DTCC), which provide regulators with information – so far limited to CDS – on deal level (i.e. including counterparties), but in the public section of their website only reveals two summary counterparty categories, “Dealer” and “Non-Dealer/Customer”, plus the respective aggregate amounts for the instrument in question. We believe this is sufficiently informative for the public, and an absolute necessity from a business secrecy point of view for corporate end-users.

CCP Requirements

Q44: Do you consider that financial instruments which are highly liquid have been rightly identified? Should ESMA consider other elements in defining highly liquid collateral in respect of cash of financial instruments? Do you consider that the bank guarantees or gold which is highly liquid has been rightly identified? Should ESMA consider other elements in defining highly liquid collateral in respect of bank guarantees or gold?

Our answer focuses on bank guarantees which non-financials, having no access to central bank money, consider as a very important alternative to cash collateral. First of all, these bank guarantees should not be restricted to non-financial “clearing members” (as the wording “are issued to guarantee a non financial clearing member” indicates) as non-financials regularly do not intend to directly access CCPs. Therefore, the term “clearing member” should be deleted.

We are also concerned that the option to provide bank guarantees is diluted by the requirement to back these guarantees with collateral that can be liquidated on a same-day basis. The additional costs occurring to the bank for the collateralisation would be passed on to their clients and disproportionally increase the prices for the bank guarantees. These costs are not justified for the following reasons: Firstly, the requirement to back the guarantee with collateral is superfluous because the risk arising from the provision of bank guarantees is mitigated sufficiently by the other requirements for bank guarantees also proposed by ESMA. Secondly, the obligation to fully back the guarantee lacks economic rationale: This would only be justifiable for the case that the whole amount of all respective bank guarantees provided by one bank is drawn from all clients at the same time. Without doubt, this is a very unlikely assumption. For this reason a partial collateral backing would be justified, but not a full collateralisation. Thirdly, for coherence reasons we would suggest to realign the collateral obligation with the Basel III / CRR rules concerning the liquidity coverage ratio which requires a **10 per cent liquidity coverage** for outstanding credit lines for non-financial companies.

The obligation that a bank guarantee should not be issued by the clearing member is also not justified as the central counterparty bears the counterparty risk and not the clearing member itself which provides only access. The exclusion of clearing members would limit the number of banks that are allowed to provide a bank guarantee for derivatives of non-financial companies as typically all banks as providers of bank guarantees are also clearing members.

Furthermore, it should be clarified what is exactly meant by “low credit risk”. We suggest to define this as “investment grade rating (foreign currency) by at least one major rating agency”.

Q47: Do you consider that the elements outlined above would rightly outline the framework for determining haircuts? Should ESMA consider other elements?

As an additional “safety net” ESMA discusses the application of hair cuts on the value of collateral. This additional requirement is not necessary because the collateral which is allowed to be posted is liquid by definition when the very strict requirements – discussed by ESMA under question 44 – are fulfilled.

Q50: Should a CCP require that a minimum percentage of collateral received from a clearing member is provided in the form of cash? If yes, what factors should ESMA take into account in defining that minimum percentage? What would be the potential costs of that requirement?

As mentioned in our answer to question 44 non-financials do not have access to central bank money. Collateralisation with cash would therefore stretch their liquidity reserves disproportionally. This should be taken into account when considering that a minimum percentage of collateral should be provided in cash. We would therefore suggest to exempt non-financials from this requirement.

Trade Repositories

Q70: Are the possible fields included in the attached table, under Parties to the Contract, sufficient to accurately identify counterparties for the purposes listed above? What other fields or formats could be considered?

ESMA should take into consideration that many non-financial, especially smaller companies have not yet implemented sophisticated reporting structures as regards their derivative transactions. Therefore, reporting requirements for non-financial companies should be proportionate. At least, non-financial companies should have the choice to delegate the reporting obligation to the selling counterparty (this is what Art. 6 para 1 EMIR states: “A counterparty or a CCP which is subject to the reporting obligation may delegate the reporting of the details of the derivative contracts”). This would also ensure that the reporting is processed without duplication.

Nevertheless, ESMA considers only a partial delegation in requiring both counterparties to deliver counterparty data (see no. 174). We are not sure if this requirement is in line with the above mentioned EMIR text. We would therefore propose to “merge” both tables, counterparty and common data, at least with regard to transactions involving a non-financial company which has not exceeded the clearing threshold. This would allow the financial counterparty to report also the counterparty data on behalf of the non-financial counterparty.

The principle of proportionality should also be considered for intra-group transactions used for hedging purposes by non-financial companies. ESMA should take into account that a delegation of the reporting requirement to a third party (especially the financial counterparty) is not possible. Therefore we would propose a lean reporting requirement for derivatives of non-financials which are used for hedging purposes. The data which is to be delivered by the respective non-financial counterparty should be restricted to the requirements laid down in Art. 6 para. 4 lit. b EMIR: Type, underlying (i.e. hedged item), maturity, notional value, price and settlement date. It should also be ensured that non-financial companies can access the respective trade repository easily.

Q71: How should beneficiaries be identified for the purpose of reporting to a TR, notably in the case of long chains of beneficiaries?

As described above non-financials often have a financial subsidiary which contracts with third parties (banks as a rule) on behalf of entities belonging to the same non-financial group. The relationship between different companies of the same group should not be regarded as a “trustee-beneficiary-relationship”. The question how to define beneficiaries should rather focus on the chain of intermediaries (economically independent from each other) and regard the group as one unit in an economically sense.

Q73: What taxonomy and codes should be used for identifying derivatives products when reporting to TRs, particularly as regards commodities or other assets for which ISIN cannot be used? In which circumstances should baskets be flagged as such, or should their composition be identified as well and how? Is there any particular aspect to be considered as regards a possible UPI?

We agree with ESMA that it is difficult to develop a taxonomy which reasonably takes into account the specifics of bespoke derivatives which are in general used for hedging purposes. From our point of view, a too granular taxonomy would disregard the specifics of bespoke derivatives, would not allow any meaningful conclusions and would cause high costs to comply with.

Q76: What is your view of the granularity level of the information to be requested under these fields and in particular the format as suggested in the attached table?

The reporting process for non-financial companies should be as lean as possible. We therefore call for the possibility to delegate the whole reporting requirement to the financial counterparty. Regarding intra-group transactions the amount of data which is to be transferred to the trade repository should be limited for non-financial intra-group transactions which are used for hedging purposes (please consider our answer to question 70).

Q78: Given that daily mark-to-market valuations are required to be calculated by counterparties under [Article 6/8] of EMIR, how complex would it be to report data on exposures and how could this be made possible, particularly in the case of bilateral trades, and in which implementation timeline? Would the same arguments also apply to the reporting of collateral?

The requirement to report the exposure and the posted collateral on a daily basis is not in line with EMIR, which requires the daily valuation only. Therefore, we do not see the mandate for ESMA to provide technical standards for this issue.

Q82: What level of aggregation should be considered for data being disclosed to the public?

We believe the same criteria should apply as proposed for intragroup transactions (see our answer to question 22). For confidentiality reasons information disclosed to the public by a trade repository should be on an aggregated level and needs to be anonym. Market participants should not be able to draw conclusions from the information publicly provided on the companies' hedging strategy or other specifics from strategic importance, either directly or indirectly.

As laid down in our answer to question 22 the example of the Depository Trust & Clearing Corporation (DTCC) should be followed. It does provide regulators with information on deal level (i.e. including counterparties), but in the public section of their website only reveals two summary counterparty categories, "Dealer" and "Non-Dealer/Customer", plus the respective aggregate amounts for the instrument in question. We believe this is sufficiently informative for the public.

Q83: What should the frequency of public disclosure be (weekly? monthly?); and should it vary depending on the class of derivatives or liquidity impact concerns; if yes, how?

The relevant metrics for public disclosures of data should not change materially in a week across the market as a whole. For example, aggregate market exposures (as opposed to individual ones) tend to change less frequently. Our opinion therefore is that monthly report updates for the public would be fully sufficient to review what is happening in derivatives markets. We would not differentiate that opinion by products.