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LSEG RESPONSE TO COMMISSION CONSULTATION ON EMIR REVIEW

London Stock Exchange Group

LSEG Response to European Commission consultation on the Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories

INTRODUCTION

London Stock Exchange Group (LSEG) is a financial market infrastructure provider, headquartered in London, with significant operations in Europe, North America and Asia. LSEG welcomes the opportunity to respond to the Discussion Paper on the European Commission's review of EMIR.

The Group operates Cassa di Compensazione e Garanzia (CC&G), the EMIR authorised CCP, and is majority owner of the multi-asset global CCP, LCH.Clearnet Group. LSEG also operates the EMIR authorised trade repository, UnaVista.

Please note that LCH.Clearnet Group Ltd has submitted its own response to this consultation and we are not responding on its behalf.

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General Comment

We welcome the opportunity to review the EMIR provisions in effect and to suggest modifications to enhance the effectiveness of these critical financial market rules. We do not believe that significant changes are required to the EMIR legislative framework and principles, which in many instances create international standards of best practice (such as the EMIR dual-sided reporting requirements). The focus of the EMIR review should be on calibrating the rules and guidelines to ensure that the operational requirements fulfil the legislative principles.

Finally, we encourage the Commission to work toward the timely completion of rules implementing outstanding EMIR requirements, in particular completing the clearing mandates and third country equivalence determinations, as well providing stewardship over the implementation of European bilateral margin requirements.

Question 1.1: CCP Liquidity

Article 85(1)(a) states that: *"The Commission shall …… assess, in cooperation with the members of the ESCB, the need for any measure to facilitate the access of CCPs to central bank liquidity facilities."*

There are no provisions under EMIR facilitating the access of CCPs authorised under EMIR to additional liquidity from central banks in stress or crisis situations, either from the perspective of the members of the ESCB or from the perspective of CCPs. However, it is recognised that in some member states, CCPs are required to obtain authorisation as credit institutions in accordance with Article 6 of Directive 2006/48/EC. Such authorisation creates access to central bank liquidity for those CCPs. On the other hand, other member states do not require CCPs to obtain such an authorisation.

i. Is there a need for measures to facilitate the access of CCPs to central bank liquidity facilities?

Yes. Access to central bank liquidity facilities is an important element of a CCP's ability to manage the various types of margin posted to it by clearing members effectively. Central bank liquidity would provide a high quality and diversified source of liquidity, helping to ensure that margin can readily be liquidised, both during a CCP's business as usual activities and during times of market stress.

Recital 71 of EMIR recognises this as a pertinent issue, but the Regulation does not include any active measures to facilitate access to such liquidity from central banks.

ii. If your answer to i. is yes, what are the measures that should be considered and why?

While EMIR does not require CCPs to obtain authorisation as credit institutions, it does have a robust procedure for the authorisation of CCPs to conduct clearing activities. The Commission should recognise that the procedure for authorising CCPs in the EU is itself an adequate basis for accessing central bank liquidity, due to the strict EMIR capital, risk management, governance and other standards that CCPs must meet. A separate authorisation for banking activities is not relevant to a CCP's activities. Therefore, we suggest that EMIR Recital 71 is amended to remove its reference to authorisation under CRD4 for access to central bank liquidity.

Further, we suggest that Chapter 1 of Title I of CRD4 should be amended to remove CCPs from the scope of CRD4. It should make clear that Member States/central banks do not need to require EMIR authorised CCPs to be authorised under Article 8 of CRD4 to access central bank liquidity (as the Eurosystem and Bank of England already provide under their respective policies) and that right of access to central bank liquidity derives from EMIR and not CRD4 authorisation.

Question 1.2: Non-Financial Firms

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

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

(a) i. Are the clearing thresholds for non-hedging transactions (Article 11, Regulation (EU) No 149/2013) and the corresponding definition of contracts objectively measurable as reducing risks directly relating the commercial activity or treasury financing activity (Article 10, Regulation (EU) No 149/2013) adequately defined to capture those non- financial counterparties that should be deemed as systemically important?

ii. If your answer to question i. is no, what alternative methodology or thresholds could be considered to ensure that only systemically important non-financial counterparties are captured by higher requirements under EMIR?

(b) Please explain your views on any elements of EMIR that you believe have created unintended consequences for non-financial counterparties? How could these be addressed?

(c) Has EMIR impacted the use of, or access to, OTC derivatives by non- financial firms? Please provide evidence or specific examples of observed changes.

Question 1.3: CCP Colleges

Article 85(1)(c) states that: *" The Commission shall….assess, in the light of experience, the functioning of the supervisory framework for CCPs, including the effectiveness of supervisory colleges, the respective voting modalities laid down in Article 19(3), and the role of ESMA, in particular during the authorisation process for CCPs."*

In order for a CCP established in the Union to provide clearing services, it must obtain authorisation under Article 14 of EMIR. EMIR introduced a college system for the granting of such authorisation, which has, to date, been used for the process of authorisation of sixteen CCPs. The College comprises members from relevant competent authorities, relevant members of the European System of Central Banks and ESMA.

(a) What are your views on the functioning of supervisory colleges for CCPs?

LSEG supports the role of EMIR supervisory colleges as a means of harmonising CCP authorisation across the EU Member States. With respect to extending a CCP's authorisation under Article 15 of EMIR, we believe that the interaction between CCPs and colleges could function more efficiently.

(b) What issues have you identified with respect to the college system during the authorisation process for EU CCPs, if any? How could these be addressed?

While LSEG strongly supports the thorough scrutiny of CCPs in the Article 14 authorisation process, we welcome a more flexible approach when extending authorisation for new

products or services. The main difficulties are the excessively long timeframe required to approve new products and the lack of clarity and consistency with respect to information required by NCAs in EU member States. This may result in a competitive disadvantage for CCPs wishing to launch new products or services. We propose the creation of ESMA guidelines which set out the criteria to determine if the additional activities or services would expose a CCP to new or increased risks.

In our view authorisation under Article 15 is appropriate, for example, in cases where the extension refers to classes of financial instruments which have a different risk profile to classes already cleared by a CCP or that have material differences from a CCP's existing authorised product set. For clearing classes of financial instruments which do not materially raise the risk profile of the CCP, (e.g. for clearing derivatives with the same category of underlying assets as those already authorized and having the same risk characteristics) we propose that a CCP should be required to issue a communication to its national competent authority only and not to the entire college. The development of guidelines specifying the parameters requiring Article 15 extension authorisation will make the procedures more predicable for CCPs and harmonised between jurisdictions.

Question 1.4: Procyclicality

Article 85(1)(d) states that: *"The Commission shall….assess, in cooperation with ESMA and ESRB, the efficiency of margining requirements to limit procyclicality and the need to define additional intervention capacity in this area."*

CCPs authorised in the Union must take into account potential procyclical effects when calculating their margin requirements. The specific factors that must be considered to avoid disruptive movements in margin calculations are provided for under Article 41 EMIR and Article 28 of Commission Delegated Regulation (EU) No 153/2013.

(a) i. Are the requirements under Article 41 EMIR and Article 28 *Regulation (EU) No 153/2013* adequate to limit procyclical effects on CCPs' financial resources?

ii. If your answer to i. is no, how could they be improved?

(b) i. Is there a need to define additional capacity for authorities to intervene in this area?

ii. If your answer to i. is yes, what measures for intervention should be considered and why?

Question 1.5: CCP Margins and Collateral

Article 85(1)(e) states that: *"The Commission shall….assess, in cooperation with ESMA the evolution of CCP's policies on collateral margining and securing requirements and their adaptation to the specific activities and risk profiles of their users."*

Collateral collected by way of initial and variation margin requirements is the primary source of financial resources available to a CCP. Title IV of EMIR and Commission Delegated Regulation (EU) No 153/2013 provide detailed requirements for the calculation of margin levels by CCPs as well as defining the assets that may be considered eligible as collateral.

(a) i. Have CCPs' policies on collateral and margin developed in a balanced and effective way?

We believe that the provisions related to portfolio margining set out in Article 41 (5) of EMIR and in Article 27 of Regulatory Technical Standard (RTS) 153/2013 could be significantly improved.

ii. If your answer to i. is no, for what reasons? How could they be improved?

We agree that the provisions set out in Article 27(1) and (2) of the RTS 153/2013 allow financial instruments to be portfolio margined if their price correlation is significant, reliable and resilient under stress and where an economic rationale exists for the price relation. We also agree with the principle that CCPs should not be required to use a particular risk-model to calculate potential losses on the portfolio, and to apply offsets.

On the other hand, we have strong concerns about the provisions concerning portfolio margining offsets under Article 27(4). We suggest an amendment to clarify the provision regarding the 80% limit on risk offset on multiple financial instruments. This would result in the rule being consistently applied in all jurisdictions.

A common interpretation of the rule is not the literal one. We believe that the common interpretation is: "*Where portfolio margining covers multiple instruments, the amount of margin reductions shall be no greater than 80%*", and the 80% refers to initial margins calculated without any offset. However, we believe that a literal interpretation is: "*Where portfolio margining covers multiple instruments, the amount of margin reduction shall be no greater than 80% of the difference between the sum of the margins for each product calculated on an individual basis and the margin calculated is an aggregated estimate of the exposure for the combined portfolio*". The 80% referred to would be the difference between margins calculated without any offset and margins calculated with the estimated aggregate offset.

We provide an example of these interpretations:

PORTFOLIO A, B: Margin(A) = 40, Margin(B)=60; Portfolio Margin (A+B)= 30

Example 1 (common interpretation)

Maximum margin reduction = 80%

*80% > [Margin(A+B+…+n)/ (Margin(A) + Margin(B)+ … + Margin(n)) – 1] *-1*

Example: 80% > [(30 / (40 + 60) – 1]-1 = 70%*

*resulting margin reduction = 70% * 100 = 70 < 80 ok*

➔ *margin called = 30*

Example 2 (literal interpretation)

*Maximum margin reduction = 80% * { [(Margin(A) + Margin(B)+ … + Margin(n)] - Margin(A+B+…+n) }*

*Maximum margin reduction = 80% * (100 - 30) = 56*

➔ margin called = 100 - 56= 44

We would be grateful if the Commission could clarify how offset applies in this example.

(b) i. Is the spectrum of eligible collateral appropriate to strike the right balance between the liquidity needs of the CCP and its participants?

We believe that certain requirements should be modified.

ii. If your answer to i. is no, for what reasons? How could it be improved?

With respect to CCP investment policy requirements for cash deposits, Article 45 (2) of RTS 153/2013 provides that when cash is not deposited with a central bank on an overnight basis, then not less than 95% of such cash, calculated over an average period of one calendar month, shall be deposited through arrangements ensuring that the collateralisation of the cash is invested in highly liquid financial instruments meeting the requirements of Annex II of RTS 153/2013 (e.g., through repurchase agreements).

We suggest reducing the 95% requirement in light of the difficulties encountered by CCPs in sourcing repurchase agreements at end of day, in particular during stressed situations. In these situations, clearing members are required to deposit daily intra-day margins thereby dramatically increasing the amount of end-of-day investable cash and intensify competition for short-term financial instruments. A review of such threshold should also be considered in light of the global trend of decreasing liquidity in short-term financing instruments. Therefore, we would suggest reducing the current 95% threshold to at least 90%, to provide CCPs with more flexibility in their cash management.

Part II – General Questions

Definitions and Scope

Title I of the Regulation contains Articles 1-2.

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

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

Question 2.1

i. Are there any provisions or definitions contained within Article 1 and 2 of EMIR that have created unintended consequences in terms of the scope of contracts or entities that are covered by the requirements?

Yes.

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

Article 1(1) states that the focus of the regulation is on OTC derivative contracts, which appears to be inconsistent with the reporting obligations under Article 9 which apply to 'any derivative' – i.e. exchange traded derivatives (ETDs) as well as OTC derivatives. We believe that Article 1(1) should be re-worded to make it clear that all derivative contracts are reportable. Further, the reporting standards should also be revised to more closely reflect the characteristics of derivatives such as ETDs.

The problems caused by Article 1(1) have been exacerbated by the definition of 'derivative' in Article 2(5), which has been interpreted in different ways by a number of National Competent Authorities (NCAs), particularly for certain foreign exchange, credit and commodity derivatives. Not only has this caused confusion amongst the reporting community, but it has contributed to the lack of pairing of reports submitted by the counterparties to a transaction (as one counterparty may believe the instrument is reportable whereas the other counterparty does not). While ESMA has been cognisant of such interpretation problems, it appears to have decided to wait until implementation of MiFID2 to address these issues. We believe that effective reporting will be compromised if the market has to wait until full implementation (and potentially subsequent guidance) of MiFID2 for clarity and uniformity. Furthermore, we note that the MiFID2 level 1 legislation and currently proposed drafts of level 2 legislation do not provide provisions to harmonise the definitions and therefore a delay is unlikely to lead to a resolution. We believe that the Commission should produce guidance in its EMIR FAQ on the boundaries of what are considered foreign exchange, credit and commodity derivatives, supported by technical advice from ESMA. This is essential to ensuring the consistent and meaningful reporting, required to monitor and identify systemic risk.

Clearing Obligations

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

Question 2.2

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

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

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

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

Trade Reporting

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

Question 2.3

i. Are there any significant ongoing impediments or unintended consequences with respect to meeting trade reporting obligations in accordance with Article 9 of EMIR?

Yes.

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

The reporting requirements appear to have been designed to report bespoke OTC derivatives, notably swap agreements, and have neglected the features of ETDs and some other types of OTC derivative (notably CFDs). Perhaps the biggest issue relating to ETDs is that they are not bespoke instruments and, as a result of their standardisation, their associated risk is considered at a ***position*** level for a particular instrument against a particular counterparty rather than at the ***trade*** level, for example on very standard positions such as equity index futures/options. ESMA has recognised the legitimacy of position reporting (as per EMIR Q&A TR17), but has not detailed how the requirements for position reporting should be undertaken and this is not currently included in ESMA's reporting standards review. This results in a lack of harmonisation across the TRs and it impacts some of the aggregations that the TRs are required to perform for public dissemination. The TRs are seeking to agree on a harmonised format in consultation with the trade associations but ESMA's participation would be useful in such endeavours.

Risk Mitigation Techniques

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

Question 2.4

i. Are there any significant ongoing impediments or unintended consequences with respect to meeting risk mitigation obligations in accordance with Articles 11(1) and (2) of EMIR?

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

Exchange of Collateral

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

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

Question 2.5

i. Are there any significant ongoing impediments or unintended consequences anticipated with respect to meeting obligations to exchange collateral in accordance with Article 11(3) under EMIR?

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

Cross-Border Activity in the OTC derivatives markets

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

Question 2.6

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

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

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

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

Transparency

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

Question 2.7

i. Have any significant ongoing impediments arisen to ensuring that national competent authorities, international regulators and the public have the envisaged access to data reported to trade repositories?

Not all NCAs have access to data within our trade repository; they have either not asked for access to the data or they have not completed the required authorisation forms. We are actively reaching out to these authorities.

We do not believe the aims of Article 81 have been fully met, due to the lack of a consistent methodology for producing public data aggregations.

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

Article 81(5) called for regulatory technical standards to ensure consistent application of Article 81. We believe that the resulting Delegated Regulation (151/2013) lacks the precision to achieve its aim. From our experience, the initial methodology for public data aggregation was not sufficiently robust, particularly with regard to the production of aggregated ETD data, which is derived from trade reports as opposed to position reports. ESMA has subsequently twice sought to develop significantly different methodologies, but even the current version remains open to interpretation. We believe the TR industry has been frustrated with this process and it is essential to meeting the objective of Art 81 that ESMA further develops its knowledge and experience required to formulate clear and robust methodology, with the assistance of the TR industry if necessary.

Requirements for CCPs

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

Question 2.8

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

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

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

ii. If your answer to i. is no, for what reasons? How could they be improved?

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

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

Requirements for Trade Repositories

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

Question 2.9

i. Are there any significant ongoing impediments or unintended consequences with respect to requirements for trade repositories that have arisen during implementation of Titles VI and VII of EMIR, including Annex II?

Yes, see comments below.

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

We do not believe that the aim of Article 72(2) regarding the proportionality of supervisory fees has been met. The Delegated Regulation (1003/2013) has a methodology that results in the apportioning of fees based on trades received and the number of outstanding trades within a trade repository, but this is not directly proportionate to the turnover of trade repository as indicated in Article 72(2). We believe that the inclusion of trade volume and outstanding trades in the calculation of fees penalises trade repositories that receive a large number of retail derivatives. Instead, we believe that the methodology should reflect the Level 1 requirement to base supervision fees on turnover, which should represent at least

50% of the calculation and that each transaction is only counted once for volume measurement, to ensure that outstanding unsettled transactions are not counted a second time (effectively as a separate transaction) when they are completed.

Additional Stakeholder Feedback

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

Question 2.10

i. Are there any significant ongoing impediments or unintended consequences with respect to any requirements or provisions under EMIR and not referenced in the preceding questions that have arisen during implementation?

Yes, in our answer below we provide our comments concerning the following issues**:**

1. Indirect clearing arrangements;
2. Regulatory capital: trading book;
3. Regulatory capital: deduction of tangible and intangible assets;
4. Clarification on regulatory capital.

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

1. Indirect clearing arrangements

EMIR allows a CCP to set up individually segregated accounts for OTC derivatives, at the request of a clearing member, in which the positions and assets of indirect clients of a client may be recorded (see Article 2 of RTS 149/2013. Under Article 3 of this RTS a general clearing member may open separate accounts for each client to allow it to distinguish in its accounts with the CCP its assets and positions from those held on behalf on its indirect clearing members. EMIR enables the clearing member to open an omnibus account under which the margin for each indirect client in the account would be calculated separately and the clearing member would be able to identify the value of collateral held for the benefit of each indirect client.

Under MiFIR provisions for indirect clearing, a clearing member that offers to facilitate indirect clearing services, if requested by the client, shall keep separate records and accounts enabling each client to: (i) distinguish in accounts with the clearing member the assets and positions of the client from those held for the accounts of its indirect clients; and (ii) distinguish in records the positions and the collateral value of the assets held for the benefit of an indirect client from those held for the benefit of other indirect clients (see Article 30 of MiFIR and draft RTS 38, Article 4(5)).

We encourage the Commission to align the EMIR and MiFIR requirements on segregation of positions and assets of indirect clients registered with the CCP to take account of MiFIR segregation requirements. We support the MiFIR provisions which allow a clearing member to open an individually segregated account at the CCP for the positions and assets of each indirect client whereas the corresponding EMIR provision seems to require, upon request of the clearing member, that the CCP should open a single segregated account for all the indirect clients of a client (see Articles 3 and 4, RTS 149/2013). We agree that a gross omnibus account segregation offering for indirect clients offers protection, however, the absence of the requirement to provide porting suggests the protection is not equivalent to that provided to direct clients. The positions and value of collateral will not be transferable to an alternate clearing broker; although porting of this type is not within the ability of CCPs as it could only occur at the clearing member/client level.

2. Regulatory capital: trading book

Investments arising from cash assets posted to the CCP as margins, default fund contributions and other resources dedicated to the default waterfall are capitalised against market risk under the EMIR framework. According to Article 4 of RTS No. 152/2013, market risk is required to be calculated on the basis set out under the 4th Capital Requirements Directive (CRD4). CRD4 requires the classification of an investment asset under the trading book or the banking book, depending upon the trading intent; positions held with a trading intent are those held intentionally for short-term resale and/or with the intention of benefiting from actual expected short-term price differences between buying and selling prices. ESMA's CRD4 Q&A No. 7 (4 June 2013) provides that while the investments held to meet regulatory requirements under Article 16 of EMIR may be held against the banking book, CCP investments based on cash assets posted as margins, default fund contributions and other resources of the default waterfall must be capitalised against market risk, because the CCP may need to liquidate them in case of a default of a clearing member.

CC&G's investments arising from cash posted to the CCP as margins, default fund contributions and other resources linked with the default waterfall under Article 45 of EMIR are intended to be held until maturity, given that the default of a clearing member is not a frequent event. We therefore suggest modifying the rule for weighting the trading book method into the market risk. We propose that the Commission either provides a different weight for assets in portfolio, instead of using the CRD4 method, or to use the banking book method for assets held in accordance with Article 4 of RTS 152/2013.

3. Regulatory capital: deduction of tangible and intangible assets

With regard to the calculation of capital requirements under Article 16 of EMIR, we suggest amending the calculation method for CCP shareholder equity. We believe that there is a lack of consistency between EU jurisdictional requirements, with some NCAs requiring CCPs to subtract from shareholders' equity published in the last annual report: First Time Adoption (FTA) reserves, available for sale (AFS) and share awards reserves, as well as the sum of tangible and intangible assets. We understand that CCPs are also required to deduct the tangible and intangible assets from the calculation of the capital calculations, in light of the greater difficulties in liquidating such assets. But we do not understand the rationale for subtracting ***tangible assets*** from capital requirements, given that these assets may be liquidated over a reasonable period of time.

We therefore suggest that the Commission confirm, either in the legislative text or in a Q&A document, the requirements for subtracting the total amount of tangible and intangible assets. We also suggest that this requirement is amended either: (i) to provide a weight to the sum of tangible and intangible assets in accordance with Article 4 of RTS 152/2013 (*i.e.*, 8% of 20%) or (ii) to subtract only the intangible assets from the shareholders' equity.

4. Clarification on regulatory capital

EMIR establishes capital requirements to ensure that a CCP is at all times adequately capitalised against credit risks, counterparty risks, market risks, operational risks, legal and business risks which are not already covered by the financial resources referred to in Articles 41 and 44 of EMIR and that it is able to conduct an orderly winding down or restructuring of its operations if necessary (see Article 16 (2) of RTS 152/2013).

In some extreme circumstances the financial resources provided under Articles 41 and 44 EMIR may not be sufficient to cover credit losses arising from clearing members' default. We understand from principle 3.4.24 of the CPSS-IOSCO Principles for Financial Market Infrastructure that "*an FMI should not include as available to cover credit losses from participant default those resources that are needed to cover current operating expenses, potential general business losses or other losses from other activities in which the FMI is engaged*". However, the main rationale for establishing regulatory capital requirements is to enable these resources to act as buffers to cover losses arising from the entity's exposure. Since the minimum capital requirements for CCPs are the very last line of defence for a CCP, we would therefore welcome a clarification on whether the CCP's regulatory capital may be used in such extreme scenarios, to address any credit losses the CCP may face as a result of any individual or combined default among its participants.