



Association des Banques et Banquiers, Luxembourg
The Luxembourg Bankers' Association
Luxemburger Bankenvereinigung

Response from the ABBL to the EBA Consultation 2012/1 On the Discussion Paper on Draft Regulatory Technical Standards on the requirement for CCPs under the Draft Regulation on OTC Derivatives, CCPs and Trade Repositories

Information about the ABBL:

ABBL ID number in the COM Register of interest representatives: 3505006282-58

Identity	Organisation
Capacity	Industry trade body
MS of establishment	Luxembourg
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Introduction and general remark

The ABBL¹ would like to first of all invite EBA to take all the reasonable time available to prepare technical measures of quality: It has always been a prerequisite for the ABBL that quality of regulation should trump speed. In this particular case, aware of the extreme pressure under which all the regulatory community currently is, the ABBL is nevertheless surprised by the fact that EBA was able to launch a consultation at a time when the ink of the EMIR regulation has not yet dried. The association understands fully the time constraints, but would like to remind not only EBA but also the other co-regulators that good quality regulation is seldom achieved with limited consultations and under pressure. The delay to respond to this vast and open discussion paper is in that sense very limited for such a key paper. Reading and responding to this discussion paper is complex because the nature of products that will be covered has an impact on the responses themselves and the attitudes users will take.

Two additional concerns are that, although answers may be found within a pure EMIR regulation approach in mind, it is not fully clear yet what would be the impact on prudential capital. What does it concretely mean to be out of EMIR (for intragroup transactions)? Does this imply that cost is also 0 for prudential matters? In the same vein, if pre-EMIR transactions are back-loaded on a TR (or not), what would happen with the capital requirements treatment of these instruments? Would they be penalised?

¹ The Luxembourg Bankers' Association (ABBL) is the professional organisation representing the majority of banks and other financial intermediaries established in Luxembourg. Its purpose lies in defending and fostering the professional interests of its members. As such, it acts as the voice of the whole sector on various matters in both national and international organisations.

The ABBL counts amongst its members' universal banks, covered bonds issuing banks, public banks, other professionals of the financial sector (PSF), financial service providers and ancillary service providers to the financial industry.

What would happen if one counterparty is willing to use a clearing house for existing derivatives? Thus, although much has been said and discussed regarding relations between CCPs and their members, there are still many open questions regarding clients of these members. Simple and basic questions are not yet addressed pragmatically. For instance, how to do reporting, who will choose clearable transactions, what information and services will these clients receive? The critical problem is that it is only when all of the regulation is known that institutions may decide to trade with members, or become members of CCPs.(?)

Finally, EMIR, through its derivative aspect, addresses a host of complex issues. This level 2 future regulation is proof that over the final word has not yet been said, neither for those who aim to be member of a CCP, nor for their clients. Yet, until approved by ESMA, they will not know which CCPs and products are eligible. Given that 5 to 6 months are likely necessary to negotiate between CCPs, their members and their clients, the ABBL strongly wonders how the deadline of 1 January 2013 could be met and accordingly calls for a grandfathering of operations under EMIR. This means that the legal framework will be effective as soon as the regulation is passed and operations will be live on CCPs or TRs once practically accomplishable.

The ABBL proposes that EBA relies on the CPSS-IOSCO standards for clearing and tailors them according to the more specific EU requirements. The ABBL also considers that some flexibility should be offered at the start of the implementation process so that the EMIR enters into force in a smooth and effective manner. Standardisation of contracts, with the fact that they will become forced to trade on negotiation platform with the MiFID II shall not be taken too lightly. Again an appropriate consultation period and broad support will be key to the success of this regulation

Specific questions

Q1. Do you support this approach to capital requirements?

The association considers that unless CPSS-IOSCO proposes a reduced alternative the best option and the most valid to accommodate the systemic risk presented by CCPs is to rely on a 12 month reference period.

Q2. Do you consider there to be any alternative approach which is more appropriate that would be consistent with Article 12 of the Regulation?

Q3. Which criteria do you take into account for estimating the appropriate time span for orderly winding down or restructuring of the CCP's activities?

Q4. What is your estimation for the number of months necessary to ensure an orderly winding-down or restructuring of the CCP's activities?

One of the key issues with the concept of winding-down is that it is inherent to at least two elements: business conditions at the time and markets in which the CCP is active. It is likely that the more stressed the environment is the longer the delay.

Then there may be again two broad scenarios under which a winding down may be envisaged, either a sudden event that threatens the existence of the CCP or that of a gradual exit of all or some activities.

Additionally, in either case, members of the CCPs would have margins, collateral and a default

fund to protect themselves. Thus, under scenario 1 of an extreme event there should indeed be a provision to ensure the CCP is able to reallocate its business. To take into account systemic risk a security margin of 12 months plus an additional 6 months should probably be sufficient. Under scenario 2 of a planned exit, it is likely that the CCP would already know that it will exit its business and need some time to sell, offer its business to a third party. Under that scenario, very close to business as usual, the reserve of 12 months is probably enough.

Because of all considerations above, a 12 + 6 months capital reserve is the most appropriate.

In any case, the ABBL considers that the definition of winding down is not clearly defined enough. For the ABBL the objective should be that the vast majority of risk has been transferred, not necessarily that 100% of the activity has been wound down. Legal proceedings or recourse on some contracts may take years to be solved even if most of the activity has been exited.

Q5. Do you think that a minimum list of items to be included in the operational expenses could be useful, such as the IAS 7?

Probably yes.

Q6. How do you currently measure and capitalise for operational risk?

No answer

Q7. Do you think that the banking framework is the most appropriate method for calculating a CCP's capital requirements for operational risk? If not, which approach would be more suitable for a CCP?

In the ABBL's view, through their deposit of margins, collateral management and default fund the business of CCPs shares some commonalities with banking activity. Thus, relying on some identical principles may make some sense. Having said this, CCPs are not banks and vice-versa.

For the association, CCPs are more than ever systemic institutions. They will concentrate the risks on derivatives instruments (among which some relatively complex,) and most regular trading of shares will go through these few systemic institutions. Thus, criteria based on the Basic Indicator Approach may be the default option as it would be the easiest one to communicate and the one that will offer the best transparency for outsiders (they may take figures and compare them to pre-defined criteria), and, finally, the option that offers the least flexibility. The latter may be to the detriment of the entire economy, as the development of new products may be more complex.

In the end, contrary to banking activity, most of the business of the CCP will be backed by either margins, collateral or default fund, which will always mitigate the direct exposure to CCP counterparty.

Specific attention should probably be given to CCP interconnectivity, where the likelihood of systemic risk spreading is increased and not supported by institutions already under the CRD framework.

Q8. What would be the cost of employing the basic indicator approach set out for banks for the calculation of your capital requirements for operational risk?

No answer.

Q9. Do you think that the Basic Indicator Approach set out for banks is appropriate for CCPs?

Please see response to Q7. In addition, there may also be some commonalities. CCPs are systemic institutions concentrated in specific segments, thus even if the Basic Indicator Approach is used it should be tailored to the specificities of CCPs.

Q10. In your view, which alternative indicator should the EBA consider for the Basic Indicator Approach? (Please elaborate why such indicator would be more appropriate for CCPs)

Q11. In your view, with regard to the Standardised Approach, which different lines of business or type of products can be relevant for CCPs' operational risk?

At least each large type of asset classes should be considered among the different business lines (shares, futures, derivatives...).

Q12. Do you think CCPs should be allowed to calculate the capital requirements for operational risk with an internal model, as in the advanced measurement approach?

Q13. Which other approaches should the EBA consider for operational risk measurement?

In line with the preference for the Basic Indicator Approach, a similar factual and public measurement should be used.

Q14. How do you currently measure and capitalise for credit, counterparty credit and market risk stemming from “non-clearing activities”?

Q15. Do you think that the banking framework is the most appropriate method of calculating a CCP's capital requirements for credit, counterparty credit and market risk stemming from “non-clearing activities”? If not, which method would be more suitable for a CCP?

Q16. What would be the cost of employing Standardised Approach methods for the calculation of your capital requirements for credit, counterparty credit¹² and market risk stemming from “non-clearing activities”?

Q17. In your view, are the Standardised Approach methods appropriate for the calculation of credit, counterparty credit and market risk a CCP faces stemming from “non-clearing activities”?

Q18. Do you think that CCPs, which concentrate risks stemming from derivatives, should be allowed to calculate their capital requirements for credit, counterparty credit and market risk using internal models?

Q19. In your view, which assets held by a CCP should be better capitalised with a market risk treatment?

Q20. In your view, which other approaches should the EBA consider for credit, counterparty credit and market risk measurement?

The ABBL generally supports the idea to rely on the CRD framework and tailor it to the CCP's need. In the ABBL's view not enough is said on the liquidity requirements, which are probably as important to ensure systemic risk management as the solvency aspects discussed above.

Q21. What is your view on the notification threshold? At which level should it be set?

Q22. In your view, in which case should restriction measures be taken by the competent authority once the notification threshold is breached?

Probably even more than under CRD or banking prudential regulation, any warning on a CCP may turn into a self-fulfilling prophecy. Every member knows how systemic CCPs are under the EMIR regulation, so that any minor increase in risk and communication on the likelihood of failure, even if indirect and very remote, will probably turn into reality. Rumours spread at an incredible speed, especially if money is involved.

Q23. Please provide the sum of the operational expenses during an appropriate time span for winding down or restructuring a CCP's activities based on the approaches specified below.

Q24. Please provide the capital requirements for operational risk.

Q25. Please provide the capital requirements for credit risk stemming from "non-clearing activities".

Q26. Please provide the capital requirements for counterparty credit risk stemming from "non-clearing activities".

Q27. Please provide the capital requirements for market risk stemming from "non-clearing activities".

Q 23 to 27 are according to the association too directly addressed to CCPs for the ABBL to respond