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|  **Division Bank and Insurance**Austrian Federal Economic ChamberWiedner Hauptstraße 63 | P.O. Box 3201045 ViennaT +43 (0)5 90 900-DW | F +43 (0)5 90 900-272E bsbv@wko.atW http://wko.at/bsbv |

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Ihr Zeichen, Ihre Nachricht vom Unser Zeichen, Sacharbeiter Durchwahl Datum

 BSBV 48/Dr. Priester/Ha 3132 14.07.14

Betrifft: **ESAs – RTS-risk mitigation techniques for OTCs**

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the consultation paper regarding “draft regulatory technical standards on risk-mitigation techniques for OTC-derivate contracts not cleared by a CCP under Article 11(15) of EMIR”:

**General Comments**

We tentatively agree with ESMA’s approach to base the suggested regime for margining requirements under EMIR on the international standards suggested by the BCBS-IOSCO framework on margining requirements for non-centrally cleared derivative transactions. We feel however, that some aspects of the suggested European framework will likely lead to unfavourable competitive positions for EU-based firms. This is especially problematic because of the high global interconnectedness of derivative markets, which could lead to important international market participants turning away from EU-financial markets and EU-based counterparties.

The introduction of mandatory margining requirements will be extremely challenging for all market participants even in the case of counterparties which are exempt from mandatory margining as they are currently designed to require a formal opt-out by contractual agreement. The rules will have extended impact on market participants which have little experience with margining of strictly bilateral transactions, and thus variation and initial margining.

The scope of derivative instruments covered under EMIR is wider than under most comparable legislations, especially the Dodd-Frank Act. The EU rules will likely mean a competitive disadvantage compared to the US and Asian jurisdictions were decisively fewer derivative instruments will be subject to extended margin requirements. This is also the reason why disproportionately strict rules on margin requirements will multiply the burden for European counterparties to non-centrally cleared derivatives on a considerable scale.

We therefor tentatively suggest that the European legislation should be tuned to continuously and consistently create a level playing field for European market participants compared to other major jurisdictions relevant for the OTC derivatives space.

The requirement for EU entities that are subject to EMIR margin rules to collect VM and (potentially) IM from non-EU entities regardless of status or size, including NFCs, central banks or sovereigns will lead to counterparties choosing to transact with non EU banks instead of EU entities which are currently active in non-EU jurisdictions without the requirement to collect margin from small scale corporates [e.g. SMEs].

We believe that it would be in line with international standards not to apply margin requirements on transactions between covered entities and non-systemically important non-financial entities and entities normally exempted from the application of EMIR.

The considerable increase in administrative costs due to the significant increase of agreements between counterparties trading OTC derivative contracts and the resources necessary to operate margin transfers on daily basis [even small FCs and their end-users] will have an impact on small end-users, who will have to rethink the way they use derivatives, even for hedging purposes. The increase in administrative and operational costs may stop small and medium sized entities hedging their interest rate risk, thereby leaving more rather than less risk in the system. If these entities seize hedging risks, the legislation would as an unintended consequence and contrary to its main objective have destabilising effects on the European financial markets and economies.

The rules on segregation of initial margins will be extremely complex and burdensome while the ban on re-use/re-hypothecation also creates a distortion of competition especially with regards to US-based banks and will hamper the derivative operations of European banks.

We also want to stress the very tight time frame of this project. We expect that counterparties will need more time to implement the requirements than close to 12 months until the mandatory compliance date on 1st December 2015 even if the rules can be implemented on time at the beginning of 2015. We believe this to be too short considering the legal, operational and documentation changes that will result from the new rules.

* **Question 2 / page 17**

*Are there particular aspects, for instance of an operational nature, that are not addressed in an appropriate manner? If yes, please provide the rationale for the concerns and potential solutions.*

1. **Exemption for intragroup transactions**

We would like to stress the importance to align the interpretation of CRR with EMIR. Therefore, transactions within a group and, based on Article 113 (7) CRR, within institutional protection schemes should automatically benefit from the relevant intragroup exemptions of the EMIR regulation.

1. **Legal impediments/non-reliance on the intragroup exemptions:**

Article 3 IGT (1) (a) and (b) mention the legal impediments to the prompt transfer of own funds which would result in the non-reliance on the intragroup exemptions. Many regulatory regimes and all insolvency, resolution or similar other regimes, by their nature, contain provisions which can affect the ability of the regulated or insolvent party or the party under resolution to effect payments or transfer assets.

We believe that "regulatory restrictions" should only be a valid legal impediment *from the moment institutions do not comply* with regulatory restrictions any more. Art. 1 IGT (1) (b) should mean that such impediment is only *deemed to exist upon initiation of such*

*proceedings* but not before.

The relevant requirement would effectively invalidate the effects of the exemption for intragroup transactions in the Regulation, which forms the legal basis of the RTS. This cannot and must not be the intention of the supervising authorities. The intragroup exemption is essential to minimize any adverse effects of and challenges posed by the application of mandatory margining to transactions between members of the same group or institutional protection scheme.

1. **Implementation of collateral transfer made of units or shares of UCITS**

We welcome the ability for the counterparties to use units or shares in UCITS as eligible collateral as it supports the need for liquidity in the markets and even if it does not benefit directly to the funds.

However, we must highlight some specific points:

* As Directive 2011/61/EU has introduced Alternative Investment Funds (AIF) as a newly regulated category of investment funds which comprises all funds but UCITS, a lot of AIF are comparable to UCITS which explains that they are often referred to as “UCITS-type” AIF. Examples in this respect are Austrian and German „Spezialfonds“ which can be held by only one investor. However such AIF will not be eligible as collateral, although they stick in principle to the same rules and requirements as UCITS. Consequently, we would appreciate if such “UCITS-type” AIF will also be considered eligible as collateral (Art 1 (1) (r) (LEC).
* Article 2 (1) (d) LEC - Collateral Management, and Article 1 (1) (i) OPE - Operational process for the exchange of collateral should take due account of the principle of proportionality. Small banks primarily access the markets through another central institution. We believe that relevant collateral management procedures should apply the principle of proportionality. EBA also recommended that smaller banks which access markets through another institution will not have to be active in several advanced money and capital markets. Thus, we support to redraft the provisions regarding collateral management procedures of the draft RTS. Similarly, the periodical verification of the liquidity of the eligible collateral (Art. 1 (1) (i) OPE) should be in the responsibility of the institution through which smaller banks access markets, but not the small institutions themselves.
* We are questioning if the exemption of exchange of collateral according to Art 2 (4) and (6) GEN comprises both initial margins and variation margins. If yes, this has not been mentioned in the chapter 3. backround and rationale.
1. **Forex financial instruments:**

We consider that foreign exchange transactions with a commercial purpose and which are physically settled should be granted the possibility to be excluded from the collection of the variation margin along with the initial one.

Regarding the variation margin: the requirements should be relevant for FX-swaps and FX-forwards, but only for deals with a settlement period beyond 3 months (below the 3 months, the counterparty risks can be considered as low, and the mitigation of the settlement risk has already been addressed by the payment-versus-payment settlement system (CLS).

Foreign exchange transactions with central banks should be exempted from EMIR requirements. Their purpose and low risk for the counterparty differ from the other Forex instruments and should be regarded as such.

1. **Post capital or hold assets**

According to Recital 3, a counterparty shall have the choice either to post / collect (initial) margins or holding own capital if the amount of initial margin is below the threshold.

Investment funds are subject to the so-called cover rule (cf. Art. 51 para. 3 of Directive 2009/65/EC as well as CESR consultation 10-108). This means, they are only allowed to enter into investments in derivatives. The obligations of such investments have to be met with the assets of the investment fund.

In order to avoid any misinterpretation, the ESAs should clarify in Recital 3 that in case of investment funds, complying with the cover rule is an equivalent to holding own capital.

* **Question 5:**

*How would the introduction of concentration limits impact the management of collateral (please provide if possible quantitative information)? Are there arguments for exempting specific securities from concentration limits and how could negative effects be mitigated?*

*What are the pros and cons of exempting securities issued by the governments or central banks of the same jurisdiction? Should proportionality requirements be introduced, if yes, how should these be calibrated to prevent liquidation issues under stressed market conditions?*

We disagree with the introduction of concentration limits. As small banks have portfolios that are to a great part made up of domestic sovereign securities, such regulation would overly penalize small institutions. As in the CRR securities issued or guaranteed by EEA Sovereigns and EEA Central Banks in the domestic currency should be considered the same way in the EMIR regulation. Concentration limits should not be applied to these securities.

Furthermore, if concentration limits are introduced, Art 7 LEC 1 (b) and (c) - concentration limits - need some further clarifications as it is not clear if the look through principle applies to UCITS funds or not (Article 7 LEC 1. (b) and (c) (page 39).

In this case we would recommend to withdraw the concentration limit for (r) [shares in UCITS], issued by a single issuer in Article 7 LEC 1. (b) (page 39). It should be possible that up to 100% of the collateral from that individual counterparty can consist of shares in UCITS as there is no counterparty risk on the issuer of the funds.

* **Question 6:**

The re-use of collateral should be allowed not only for transactions cleared with CCPs but also for non-centrally cleared transactions provided that it is limited to certain type of instruments.

Yours faithfully,

Dr. Franz Rudorfer

Managing Director

Division Bank and Insurance