



EBA Consultation on Draft Guidelines specifying the conditions for the application of the alternative treatment of institutions' exposures related to 'tri-party repurchase agreements' set out in Article 403(3) of Regulation (EU)575/2013 for large exposure purposes

Euroclear response

Euroclear welcomes the EBA consultation related to tri-party agreements in the frame of the Large Exposures regime. We appreciate the possibility to provide our views on this important topic and trust that EBA will take them into account. You will find below the response of Euroclear Bank ('Euroclear') to the questions formulated by the EBA. Euroclear is hereby responding in its capacity as tri-party agent.

The Euroclear group is the world's leading provider of domestic and cross-border settlement and related services for bond, equity and fund transactions. The Euroclear group holds assets under custody for a value of €31 trillion and settled transactions for a value of €837 trillion in 2019. Largely user owned and user governed, the group includes the International Central Securities Depository (ICSD) Euroclear Bank, based in Brussels, as well as the national Central Securities Depositories (CSDs) Euroclear Belgium, Euroclear Finland, Euroclear France, Euroclear Nederland, Euroclear Sweden and Euroclear UK & Ireland.

Although we believe that the alternative treatment proposed in the Consultation may be an alternative for institutions to report indirect collateral exposures under CRR, we would like to highlight three points on which we request EBA to reconsider its proposals:

The first is that reporting a limit instead of the actual exposure means it is assumed that the full limit is used in the calculation of the total exposure whilst this will likely not be the case. It may therefore lead to an exaggeration of the exposure calculation and reporting, and depending on the type of institution, their business, and capital, not an optimal solution. This problem is exacerbated by the fact that institutions typically have exposures across multiple businesses, and multiple Triparty Agents. As indirect collateral exposures breaches would typically tend to occur on higher quality assets (with a lower or equal risk weighting to the



counterparty, we believe that there could be an unintended consequence that institutions will need to restrict to receive such assets whilst lower quality assets will still be accepted. Therefore we would recommend that rather than imposing to manage the indirect collateral exposures ex ante through the reporting and implementation of limits, to monitor collateral holdings and react and take action when there is a breach. Triparty Agents provide all necessary tools to their clients to monitor their collateral holdings. This point is further detailed in our response to Question 2.

The second point is that we would like to ask the EBA to revisit its approach on the definition of limits based on (bespoke and static) groups of issuers. As we currently understand the alternative treatment, institutions may have to move away from the current dynamic approach to set limits at issuer / asset class level, and instead create limits on static lists of issuers that institutions would need to provide the Triparty Agents with. This point is further detailed in our response to Questions 5 and 7.

Thirdly, we would like to point out that a Triparty agent like Euroclear offers collateral management services on many different underlying collateral transactions such as but not limited to repurchase transactions. Other underlying exposures that are managed include securities lending transactions, exchange of initial margin for OTCD transactions, etc We believe that the approach may be useful for other exposures falling under CRR2, and not only for repurchase transactions.

Q1: Are the definitions and their use throughout the guidelines clear?

Response:

We hereby provide some comments on the definitions of Tri-party repurchase agreement, and Tri-party Agent. We would also like to point out that a Triparty agent like Euroclear offers collateral management services on many different underlying collateral transactions such as but not limited to repurchase transactions. Other underlying exposures that are managed include securities lending transactions, exchange of initial margin for OTCD transactions, etc...We believe that the approach may be useful for other exposures falling under CRR2, and not only for repurchase transactions.



As to the Definitions we would like to recommend the following nuances:

- Tri-party repurchase agreement means a repurchase transaction where the counterparties appoint a tri-party agent to act as their agent and facilitate collateral management services during the execution of tri-party transactions;
- Tri-party agent means a third party that executes collateral management services which may include payments and/or delivery of securities, safekeeping and administration services of securities including collateral selection, custodianship for the account of the counterparties to a tri-party transaction.

Q2: Do you think that this general framework is appropriate? Are there other elements that should be included to make the service agreement more comprehensive?

Response:

We would like to highlight that reporting a limit instead of the actual collateral exposure means it is assumed that the full limit is used in the calculation of the total exposure while this will likely not be the case. It may therefore lead to an exaggeration of the exposure calculation, and depending on the type of institution, their business, and capital, not an optimal solution. As most institutions have multiple exposures to monitor across different businesses either bilaterally (they allocate themselves the collateral used as mitigant for the exposure), or through multiple Triparty Agents, reporting the limits with those different Triparty Agents may lead to a highly exaggerated picture vs the real exposures.

In addition, given that indirect exposures breaches would typically tend to occur on higher quality assets (with a lower or equal risk weighting to the counterparty), we are concerned that the only way to achieve this ex-ante across multiple counterparties, multiple exposures (SFTs, OTCD, ..), multiple providers, bilateral vs triparty, etc, would mean to limit the possible usage of very good collateral/issuers to a small number or amount, i.e. forcing substitution of better quality collateral with lower rated collateral. In our view, there could thus be an



unintended consequence that institutions will restrict to receive such assets whilst lower quality assets will still be accepted.

We therefore would recommend that rather than imposing on institutions to manage the indirect collateral exposures ex ante through the imposition and reporting of limits with the Triparty Agents, that they monitor collateral holdings and react and take action when there is a breach. Triparty Agents provide all necessary tools to their clients to monitor their collateral holdings, and to take action either on bilateral activity (for which institutions control the collateral allocated themselves), to reduce their exposure or to adjust criteria in some of the triparty trades if needs be.

The Euroclear Triparty Service Agreement is constituted of the Terms and Conditions, outlining the rights and obligations of each party; of the Operating Procedures, outlining the functioning of Euroclear's triparty collateral management services; and of the Annexes (aka Collateral Profiles), in which the eligibility criteria, concentration limits and haircut or margin requirements agreed by the parties are documented. The Service Agreement contains most of the elements proposed in the Guidelines.

Euroclear makes different types of collateral reporting available to clients. These reports can be provided multiple times per day or at the end of the day (at the option of the client). They provide detailed information on the collateral received including the ISIN code of the collateral securities, the name, the market value.

Institutions or third parties such as their auditors or competent authorities can verify at any point in time compliance of the collateral received vs instructed limits, on the basis of the collateral reporting.

Q3: Do you agree with the list of proposed safeguards? If no, please explain why and present possible alternatives.

Response:

We have no particular comments on the list of proposed safeguards.

On an annual basis, Euroclear provides its clients with an ISAE 3402 type II report, designed to provide third-party assurance on the controls and procedures of Euroclear Bank. The report includes substantial information on Euroclear Bank's



internal controls and procedures, and results of testing performed by independent auditors. Amongst others, independent auditors check for a sample of contracts that the requirements of the clients are correctly reflected in the triparty collateral management system. We are of the view that this report should be the appropriate vehicle that can be used to comply with the annual declaration requirement, and the right for institutions to verify the Triparty Agent's compliance with the safeguards as described in the guidelines.

Q4: Do you see any practical reasons that would prevent the implementation of any of the safeguards? If yes, please explain.

Response:

We believe it would not be practical to request the Triparty Agents to allow audits by individual firms to verify compliance with the safeguards. As stated above, we believe that the annual ISAE 3402 type II report or a similar standard report should achieve the same objective.

Q5: Do you consider that the criteria listed in this section, in particular in paragraph 18, provide a sufficient guidance for institutions to determine limits? Are there any other elements that would be useful to include?

Response:

We believe the criteria provide sufficient guidance for the institutions to determine the limits. However, as we currently understand the alternative treatment we believe the institutions may have to move away from the current dynamic approach to set limits at issuer / asset class level, and instead create limits on static lists of issuers. Indeed, even if the guidelines mention that limits can be defined at security type level, we understand that the Guidelines would require institutions to provide the Triparty Agents with lists of connected issuers which could be based on different (customised rather than standard) criteria, and possibly no shareholding.

A Triparty Agent is alleviating both administrative and operational tasks involved in collateral management. Through automation and standardization, market participants can benefit from a reduction of market risk (through centralization of



thousands of collateral schedules, more frequent mark-to-market of the collateral and increased collateral diversification) and a reduction of operational risk (through end-to-end straight-through-processing and automation).

We believe that the EBA proposal of creating and maintaining 'bespoke' or 'customised' lists of static data will be detrimental to the performance of the current Triparty arrangements as it will be cumbersome, not standardised and not transparent to counterparties. We would advise EBA to revisit its approach on this topic.

In the Euroclear triparty environment, when setting up the collateral service agreement, institutions will define collateral profiles which include the definition of which asset classes clients have agreed to make eligible for their triparty activity. Euroclear indeed allows its clients to implement exclusions and limits in their Collateral Profiles. Such parameters can be set at the level of any collateral criterion supported by Euroclear. These include, but are not limited to: the issuer type, the index, the issuer country, the issuer nationality, the rating, the instrument type, etc.

Exclusions and limits can be set up at issuer level, or a 'family of issuers'. Though restrictions can be set on specific issuers, they are more commonly applied to *any* individual issuer (e.g. the value of all positions issued by any individual issuer of a certain type (AA rated, or a certain sector) cannot exceed € 50 million equivalent) because it is difficult for the Collateral Taker to anticipate all the issuers whose securities he might receive. As part of its triparty collateral management service, Euroclear automatically checks all the limits applicable to a security prior to allocating it as collateral in a triparty transaction.

Triparty Agents will maintain information on 'Families' of securities, and this based on standardised information. For example, securities will be considered to be part of the same Family as soon as one company has a stake of 50% or higher in another.

Q6: Is it clear to you how to apply a 'margin of conservatism' as set out in paragraph 19?

Response :

Yes, this is clear.



Q7: Do you think that applying the same criteria for the alternative treatment is a suitable method? Do you consider that there could be alternative ways?

Response:

We request EBA to revisit its approach for the following reasons: in our role as Triparty Agent we aim, among other things, to alleviate both administrative and operational tasks involved in collateral management, and thus to reduce operational risks, bring operational efficiencies, and reduce operational cost.

We do believe it would be better that, in the context of a triparty service agreement, limits – whether in absolute amounts or in percentage - are expressed at issuer type or asset class level instead of by individual issuer or group of issuers. In addition, we believe it would be better to define groups of connected issuers on the basis of standardised data available to the entire market, rather than building bespoke groups of issuers that are different for each counterparty.

We are concerned that defining limits on lists of specific issuers, and building customised groups of issuers, will lead to increased costs for both the firms and the Triparty Agents, and will reduce standardisation and transparency.

Q8: Do you agree with the general approach for the revision of the instructed limits? Is this approach appropriate in the context of general revisions of concentration limits and exclusions that currently govern the relationships with tri-party agents?

Response:

We agree with the general approach for the revision of instructed limits and believe it is appropriate in the context of general revisions of concentration limits and exclusions that govern the relationships with Tri-party agents.

Revisions of limits are possible at any time during the lifetime of the service agreement to the extent both parties to the triparty agreement with Euroclear have agreed to the amendment (except for the exceptional cases where amendments can be made unilaterally).



Q9: Do you agree with the general approach regarding when the limits need to be revised?

Response:

Yes, we agree with the general approach regarding when the limits need to be revised. A dynamic revision of the limits during the lifetime of the service agreement is possible. The implementation time will depend on the number and the relative complexity of the requested changes, and the criticality of the request.

Q 10: Do you think that the guidelines represent an appropriate approach to the monitoring of the instructed limit and in general of the implementation of the alternative treatment?

Response:

Yes, the guidelines represent an appropriate approach to monitoring limits.

We would just like to point out that Euroclear will not automatically trigger revisions of limits when these are breached, but rather correct the breach by adjusting the collateral composition. A revision of the limit is an amendment to the triparty service agreement which typically requires the consent from both parties to that agreement.

As per our answer to Question 5, as part of its triparty collateral management service, Euroclear automatically checks all the limits applicable to a security prior to allocating it as collateral in a triparty transaction. Also, during the life of the transactions, Euroclear constantly (more precisely on a hourly basis) monitors the applicable limits and triggers in an automatic way movements that would be required to keep the allocated collateral within the limits. Practically, in the rare event a limit is found to have been breached, Euroclear will automatically in the next hour trigger the processing of a substitution of collateral with the objective to replace the securities collateral allocated leading to the breach of the applicable limits, with other eligible securities collateral of a different 'Family' of issuers, in order to correct the breach and remain within the limits as set forth in the triparty service agreement.



Q11: Do you think that tri-party agents have in place such controls that would facilitate the management of the instructed limits? Would you assess that the control mechanisms should be more precise and prescriptive?

Response:

The Euroclear control environment is able to correctly monitor the instructed limits, to detect breaches, and to correct these, as described in our answer to Question 10, by triggering within the next hour a substitution movement replacing the securities collateral triggering the breach by other eligible securities collateral (of a different 'Family' of issuers). Breaches of limits are not only rare, in addition, they will be solved very quickly.

Euroclear provides continuous collateral management reporting to its clients (i.e. both collateral givers and collateral takers). Such reporting includes detailed views on the collateral allocated to triparty transactions as well as the collateral movements that have settled between collateral giver and collateral taker accounts. These reports are sent via Swift, File Transfer and/or email and are also available via our user interfaces, namely EasyWay. The exact frequency depends on the reporting channel the client opted for.

Q12: Do you agree with the non-exhaustive list of material concerns?

Response: We do not have particular comments on this question.

Q13: Are you aware of any other material concerns to be included in the guidelines?

Response: We are not aware of other material concerns to be included in the guidelines.

Q14: Do you see a need for further clarification of the procedure dealing with a material concern?

Response: We do not have particular comments on this question.



Q15: Please specify what overall impact the proposed procedure would have on expected practices.

We would highlight that changing from the alternative approach to the standard one will be difficult for an institution to achieve upon short notice, and that some transition time will be required.

For more information, please contact:

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