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DUFAS response on the EMIR AAR Consultation

To	ESMA (cc AFM)
From	DUFAS (the Dutch Fund and Asset Management Association)
Date	27 January 2025
Subject	**ESMA Consultation Paper, Conditions of the Active Account (ESMA91-1505572268-3856)**
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Introduction

The Dutch Fund and Asset Management Association (**DUFAS**) welcomes the opportunity to respond to the ESMA Consultation Paper, Conditions of the Active Account (ESMA91-1505572268-3856), as published 20 November 2024.

General comments

DUFAS and its members fully support the principle that demonstrating compliance with the conditions to meet the Active Account Requirement ("**AAR**") should not impose excessive additional costs on market participants. However, we remain concerned about the operational and financial burdens posed by the additional information requirements under EMIR 3.0 AAR and the need for supervisors to reassess existing information differently. These challenges risk increasing costs for both the industry and supervisors. As such, we believe that the standardization of reporting requirements, as highlighted by ESMA in its consultation, is a critical prerequisite for the proposed obligations.

In this context, DUFAS and its members seek to provide constructive input on specific elements of the consultation, particularly those related to derivative classifications, reporting requirements, and the reference period for AAR application.

We are concerned about the amount of additional information that must be provided under the EMIR 3.0 AAR by market participants and the existing information that will have to be reviewed differently by supervisors. Both these factors increase the operational pressure on both the industry and supervisors and will lead to additional costs. The standardization of reporting requirements, as noted by ESMA in the consultation, is therefore in our view a necessary precondition for the proposed reporting obligations.

Additionally, DUFAS and its members note that the current breakdown of derivatives contract classes and subcategories does not reflect market practise. When considering the choice of maturities and volumes, members of DUFAS are almost exclusively involved in derivatives contracts with maturities of more than 15 years and volumes exceeding €50 million. For shorter maturities, smaller sizes are not particularly relevant for market participants exceeding the €6 billion threshold. Therefore, DUFAS and its members would like to advocate for fewer categories based on size.

There are still some ambiguities regarding expectations when fewer than five relevant subcategories exist with a non-zero number of trades. Additionally, the exclusion of trades at an EU CCP is not entirely clear. In our view, ESMA should provide numerical examples to enhance clarity and support a more consistent interpretation.

Finally, DUFAS and its members are of the opinion that the reference period of six months used for application of the AAR should be extended to one year. While clients of the members of DUFAS may quickly reach large notional amounts, this is not reflected in terms of trading activity. In some cases, only one trade may occur in six months. If a reference period of 6 months is used, additional transactions will have to be entered into in order to meet the requirements.

DUFAS and its members appreciate the opportunity to contribute to this consultation and support the objective of fostering transparency and consistency in derivatives reporting under EMIR 3.0. We believe that addressing the concerns outlined in this response, particularly around reporting standardization, derivative classifications, and the reference period, will help ensure a more proportionate and effective framework.

We remain committed to constructive dialogue and collaboration with ESMA and other stakeholders to refine these proposals. DUFAS and its members are available to further discuss our perspectives and assist in aligning regulatory requirements with market practices to achieve shared objectives efficiently.

Our responses in detail

1. **Are there any aspects of the AAR scope on which ESMA has based its quantitative analysis and its policy choices that ESMA should consider detailing further*?***

   In general, DUFAS and its members would like to note that the current scope gives the impression that the gross notional thresholds have been particularly calibrated based on banks with high (cleared) swap turnover, in particular investment banking activities. Many market participants have reached their current gross notional amount over the course of more than 8 years (since the clearing obligation came into effect), and most of their hedging activities vs current positionings are incremental in terms of additional trade tickets and gross notional amounts.

   We also note that not all market participants can automatically or periodically compress their cleared swap book due to accounting, solvency or corporate tax constraints in order to steer below the € 6 billion and € 100 billion thresholds respectively. This could vastly inflate their gross notional amount, in particular if they only steer their balance sheet based on net DV01 and key rate risk regardless of the gross notional amount and number of swaps outstanding. For market participants with less derivatives turnover, a holding/exposure-based threshold, such as on total cleared DV01, would be more appropriate and easier to monitor and manage.

From the perspective of some of the clients of DUFAS's members such as insurance companies, we also note that the liabilities discount curve prescribed by EIOPA will still be solely based on the LCH swap curve in the near future. Any qualitative or quantitative AAR which obligates market participants to increase clearing activity at EU CCPs may thus increase the basis risk between the aforementioned Tier 2 CCP and the EU CCP (which has different fixed swap rate compared to LCH depending on their tenor). DUFAS and its members would therefore like to encourage ESMA to liaise with EIOPA in order to streamline a gradual transition to EU CCPs without creating undue (temporary) basis risk between swap curves which could hurt the Solvency II ratio of insurance companies with longer dated liabilities. Not coordinating these requirements and timelines simply means that insurance companies would be stuck between a rock and a hard place, and may enter into (nearly) fully offsetting swap trades at the same EU CCP in order to neutralize the DV01/key rate risks of prior swap trades cleared within the respective AAR measurement period just for the sake of EMIR compliance.

In addition to these general points, DUFAS and its members would like to address some specific aspects of the AAR scope that should be clarified.

- *85% exemption*

Firstly, DUFAS and its members are of the opinion that the proposed 12-month look-back period for the exemption threshold of 85% in section 3.4 (based on the aggregate month-end average position) could hinder the ability of market participants to benefit from this exemption, especially if they have recently shifted their clearing activity to an EU CCP. The proposed timeframe could result in market participants failing to qualify for the exemption, even though they have already moved most of their clearing to EU CCPs. In such cases, market participants would still need to set up systems to monitor trades across multiple CCPs, perform stress-testing, and meet reporting obligations, which is counterproductive.

Most importantly, Level 1 of the EMIR 3.0 text does not suggest a look-back period. It seeks to provide an exemption to market participants that are '*already clearing*' a significant amount on an EU CCP. According to Recital 13, the rationale of this exemption is to allow market participants to gradually adopt this novel requirement. Such a migration, however, will require a complex reallocation of clearing activity. Few market participants that today clear most of their trades at a Tier 2 CCP will be able to move significant volume into the EU in such a short time frame to benefit from this exemption. This is particularly challenging for buy-side firms, as they are generally small market participants with limited clearing activity, and their onboarding may not be prioritized by clearing brokers if bottlenecks occur following significant migration of activity into EU CCPs.

To ensure that market participants are able to avail themselves of the 85% exemption, DUFAS and its members suggest that the methodology for the calculation of the exemption threshold should be aligned with the EMIR 3.0's effective dates and timelines. The period which the first calculation covers should not start before EMIR 3's entry into force (i.e., 24 December 2024). This may be achieved either by allowing market participants to conduct the calculation 6 months following the effective date of the RTS on operational conditions with a 12-month look-back period, or by applying a shorter look-back period of for example 6 months (the look-back period covers 24 December 2024 to 25 June 2025). Another alternative would be to apply a shorter look-back period of for example the aggregate month-end average position for the 15 days leading up to the AAR coming into effect. If this is not done, market participants that would have been able to reach the 85% threshold may fail to qualify for the exemption because of the look-back period commencing before the official publication of EMIR 3.0.

Additionally, ESMA should confirm that market participants clearing 85% of their derivatives on an EU CCP automatically meet the representativeness requirement, as this would remove unnecessary monitoring and reporting burdens. These adjustments would make the 85% exemption more practical and encourage market participants to clear more trades on EU CCPs.

- *Notification timeline*

Secondly, DUFAS and its members request confirmation regarding the timeline for notifying NCAs about the opening of an active account. It is currently unclear whether market participants are required to notify their respective NCA about the application of the AAR already. DUFAS and its members believe that this deadline should be set on June 2025, so that it aligns with the submission of results from the clearing obligation calculations under the current EMIR Refit cycle, as well as the date on which the AAR comes into force and the first batch of active accounts is expected to be opened. This alignment would streamline compliance efforts and reduce unnecessary operational burdens for market participants.

- *Group entities*

Thirdly, DUFAS and its members would welcome confirmation that market participants within a group subject to consolidated supervision, with zero trades in paragraph 6 derivatives, will not be required to open an active account, even though the group-level calculation may exceed the threshold.

Also, DUFAS and its members find it important to note that a '*centralised treasury*' model as mentioned in paragraph 3.3.40 is not practical for smaller market participants. Therefore, we are of the opinion that it must be clarified that market participants with zero trades in paragraph 6 derivatives are not required to open an active account <u>under any circumstances</u>.

- *Treatment of STIRS*

Fourthly, in relation to paragraph 32, DUFAS and its members request confirmation on the following interpretation. Based on the current drafting, our interpretation is that as STIRs cleared on a regulated market are excluded from the clearing obligation calculation, a market participant with more than € 3 billion in gross notional value in STIRs on a regulated market, but less than the clearing thresholds in any relevant asset class would fall outside the scope of the AAR. We are of the opinion that amending the text to state that the market participant '*will fall out of the obligation to hold an AA in the EU*' adds more clarity.

- *UK STIRS traded at ICE EU*

Lastly, DUFAS and its members would like more clarity on whether UK STIRs traded at ICE EU would be treated as OTC and, therefore, would be added to the EUR swap notional amount when calculating totals.

2. **Do you agree with the above approach for condition (a)? Are there other requirements that ESMA should consider for meeting condition (a)?**

DUFAS and its members are concerned with Article 1(c) of the draft RTS where it refers to '*with sufficient financial resources to meet the obligations arising from the direct or indirect participation in an authorised CCP*'. As per paragraph 67, operational capacity is distinct from and should not include market participants' financial resources. As such, the availability of financial resources on cash and collateral accounts is not constitutive for operational capacity. Furthermore, this implies that market participants are required to have financial resources available for stress-testing purposes under Article 3 of the RTS.

Additionally, we are of the opinion that showing a (portfolio) of cleared trade(s), should already be evidence of active contracts and IT infrastructure. More specifically, cash and collateral accounts will already be in place when market participants are active on a CCP. Therefore, reporting on or providing proof of this is overly burdensome and should not be obligatory. We would furthermore like to note that if the operational infrastructure and portfolio management/trading activities are highly decentralized within an EMIR consolidation group (i.e. delegated to local subsidiaries). Coordination and ensuring group-wide AAR compliance in real-time will therefore be rather challenging.

3. **Do you agree with the above approach for conditions (b) and (c)?**

DUFAS and its members are of the opinion that the responsibility for producing and providing a written statement should fall on the CCP, as the regulatory burden should be with the CCP, and not the clearing member and/or end-clients. We note that many market participants do not have a direct CCP membership, but clear through clearing members. These clearing members often apply total (net) DV01 or initial margin limits per client that are applied to both total holdings and the incremental DV01/initial margin increase within a single trading day. The stress test may implicitly require some mid- and large sized market participants to start onboarding multiple clearing members (and bear the associated additional operational and cost burden) for access to the same EU CCP in order to have sufficient clearing capacity to meet the stress test.

Additionally, DUFAS and its members do not agree on the threefold increase in derivative portfolio positions as the impact for market participants with a very limited position in an EU CCP (for whom such a stress test might be most relevant) is minimal, whereas for market participants with a substantial share in an EU CCP, this results in unrealistic positions that are disproportionate to the interest rate risk such a market participant seeks to hedge. A more appropriate approach would be an absolute increase of, for example, 25 percentage points.

Finally, DUFAS and its members believe that the requirement under Article 2(1)(b) of the draft RTS to assign a single person responsibility for the '*proper functioning of clearing agreements*' is impractical. Large market participants typically distribute the management of clearing agreements across multiple roles, with different individuals overseeing specific aspects of the process. Centralizing this responsibility to a single person would not align with the operational structure and division of expertise within such organizations and would impair the flexibility of market participants to decide how to embed expertise with respect to these clearing arrangements in their organisation. We also note that EMIR does not require individuals with knowledge to support clearing arrangements to be identified, while EMIR mandates central clearing. Furthermore, market participants are already subject to robust governance frameworks and requirements that ensure all relevant individuals involved have sufficient knowledge and expertise. Introducing this additional requirement would therefore add little to no value while complicating established practices.

4. **Do you agree with the proposed approach for the annual stress-testing conditions (a), (b) and (c)?**

DUFAS and its members believe that stress testing, including the simulation of an 85% increase in total outstanding activity for the active account, should be conducted solely between the clearing member and the CCP. This approach ensures that the responsibility for managing clearing risk remains with the market participants directly involved, without imposing unnecessary operational burdens on other market participants. Additionally, we are concerned that sharing all outstanding positions with the clearing house could result in the disclosure of competitive information. Therefore, it is preferable for the information to be exchanged only between the clearing member and the CCP.

ESMA's proposal to conduct stress tests over five liquidation days raises concerns. We believe it would be unrealistic to trade such a large volume in the market within this short time frame, making the exercise unrepresentative of a real-world scenario. Finally, we find that stress-testing the conditions is redundant, as the conditions themselves already serve as a de facto stress test for the normal use of the active account.

5. **Do you agree with the differentiated frequency for the stress-testing depending on the counterparties' clearing activities? Would you suggest any other way to take into account the proportionality principle?**

   No comments.

6. **Do you agree with the proposed classes of derivatives for EUR OTC IRD?**

   DUFAS and its members would like to note that for market participants who predominantly trade IBOR-based swaps, and only occasionally trade a RFR-based swaps (to manage the RFR-6M Euribor basis and Discount 01), satisfying the representatives requirement of the additional class (and tenors/sizes) would be hard, especially when measured in monthly intervals. It also has the side effect mentioned in our response to Q9. We therefore propose merging these two classes as their nature and risk is not materially different despite having a different floating reference rate.

7. **Do you agree with the proposed classes of derivatives for PLN OTC IRD?**

   No comments.

8. **Do you agree with the proposed classes of derivatives for EUR STIR?**

   No comments.

9. **Do you agree with the proposed maturity and trade size ranges for each class of derivatives in EUR OTC IRD?**

   DUFAS and its members do not agree with the proposed maturity and size ranges as this would artificially inflate the number of trades since a larger notional can be split into 2 or more smaller tickets in order to satisfy the representativeness requirement. Additional swap tickets increase the administrative/trading burden, and operational costs charged by custodians, back/mid office and clearing members. It also doesn't distinguish between short dated and longer dated swap tenors, as the same notional in the latter has a much larger DV01/risk contribution.

   A potential side effect of these maturity and size ranges is that it will be hard(er) to make an ex-ante estimate of meeting the clearing obligation for various buckets/classes. Some market participants may opt to clear their first executed trades during the measurement period at an EU CCP and trade the remainder of their swaps within the same measurement period at a Tier 2 CCP. Even though the current AAR was presented as a qualitative account requirement by ESMA, this is implicitly moving towards a rather stringent quantitative requirement especially if applied to a 1-month measurement period.

10. **D o you agree with the proposed maturity and trade size ranges for each class of derivatives in PLN OTC IRD?**

    No comments.

11. **Do you agree with the proposed maturity and trade size ranges for each class of derivatives in EUR STIR?**

    No comments.

12. **Do you agree with the proposed number of most relevant subcategories for each clearing service of substantial systemic relevance? Do you think this should be set at a more granular level (i.e. per class of derivatives)?**

    DUFAS and its members are of the opinion that the bucketing approach is too granular for market participants with low turnover who have a relatively large steady state swap portfolio in longer dated swaps (such as pension funds and insurance companies). We therefore propose merging the IBOR and RFR derivative classes given their similarity, and removing the trade size bucketing.

13. **Do you agree with the proposed reference periods for EUR OTC IRD? Do you think the reference periods should be set at a more granular level (i.e. class of derivatives)?**

    DUFAS and its members are of the opinion that a yearly approach should also be sufficient regardless of whether a market participant have over EUR 100 bn gross notional or not, to avoid putting an undue burden on market participants in terms of artificially inflating cleared swap trade volumes and transaction monitoring.

14. **Do you agree with the proposed reference period for PLN OTC IRD? Do you think that the reference periods should be set at a more granular level (i.e. class of derivatives)?**

    No comments.

15. **Do you agree with the proposed reference periods for EUR STIR referenced in Euribor? Do you agree with the proposed reference periods for EUR STIR referenced in €STR?**

    No comments.

16. **Do you agree with the proposed approach for the reporting of the activity and risk exposures of the counterparty subject to the active account requirement?**

    DUFAS and its members disagree with the proposed approach to reporting the activity and risk exposures of market participants subject to the AAR. Trade repository data is already collected, meaning that ESMA and the NCAs already have access to the necessary information. This is also acknowledged in the Consultation Paper itself, specifically in paragraph 164, where the ability to cross-reference with the tables under Delegated Regulation 2022/1855 is mentioned.

The current proposal undermines the objectives of EMIR Refit, which aim is to simplify and streamline reporting obligations for market participants. Furthermore, given the lack of standardization compared to the current Article 9 reporting, this additional reporting would offer limited value, as it would not facilitate the generation of automated, comparable reports across different jurisdictions.

17. Do you consider that including information on margin activity in the AAR reporting requirement would provide valuable information on the activities and risk exposures of the counterparty?

DUFAS and its members disagree with the proposal, as we believe that showing an active portfolio should be sufficient for supervision. Both variation margin and initial margin must be transferred to the CCP as a prerequisite for trading activity, so reporting these figures would not provide significant supervisory value.

Moreover, CCPs may offer multiple clearing models, such as EUREX ISA Direct and EUREX Cross Margining. Even with the same trading activity (outstanding positions), these models can generate different initial margin requirements, making reporting on initial margin for OTC cleared interest rate derivatives cumbersome. For example, EUREX Cross Margining provides netting benefits between futures/options and OTC cleared interest rate derivatives, meaning that reporting initial margin requirements separately for OTC cleared interest rate derivatives is not feasible.

Additionally, haircuts on non-cash collateral used for initial margin are determined by the CCP and can change on an ad-hoc basis. In addition to the initial margin from the CCP, market participants also may have agreed to an operational buffer, and a clearing member may use additional collateral amounts (multipliers). If the aim is to report on variation margin (which has no haircuts) and initial margin (where haircuts apply only to non-cash collateral), we recommend using current market values for variation margins and requiring clearing members to report on initial margins.

18. Do you consider that including reporting on Unique Trade Identifiers (UTIs) would provide valuable information from a supervisory perspective?

No comments.

19. Do you agree with the proposed approach for the reporting of the operational conditions?

DUFAS and its members are of the opinion that Article 8(1)(b) is unnecessary, as it requires reporting on material changes to internal policies, systems, and governance, which does not add additional value for the purpose of the AAR. The active account, by definition, is a standard clearing account, and reporting should confirm that proper clearing arrangements are in place through a clearing member at an authorized EU CCP, which should be assumed to be operationally fit for purpose. The current broad interpretation of '*material changes'* creates an onerous compliance burden without any benefit. Especially since NCAs already have the possibility to request information from market participants.

Similarly, and in line with our answer to Q2, Article 8(1)(c)(i), requiring account statements for cash and collateral is redundant. When a clearing agreement is in place with a clearing member, sufficient clearing limits are already established to comply with EMIR pre-trade clearing requirements. Requiring additional account statements introduces unnecessary obligations not specified in the Level 1 text. Article 8(1)(c)(ii), which mandates reporting staff names and contact details for ensuring proper functioning, is also unnecessary. The responsibility lies with the company, not individuals. A certification of dedicated staff would suffice, and requiring names would lead to frequent updates, which is impractical.

For these reasons, we propose removing Article 8(1)(b) and (c) from the draft RTS, as the remaining obligations in Article 8 already fulfil the requirements of the Level 1 text.

20. **Do you agree with the proposed approach for the reporting of the representativeness obligation?**

DUFAS and its members are concerned about the reporting requirements outlined in Article 9 of the draft RTS, particularly the need to report '*gross and net notional amounts cleared*' for each subcategory and class of derivatives at both third country CCPs (Article 9(1)(b)) and EU CCPs (Article 9(1)(b)). This requirement seems to duplicate the reporting of activities and risk exposures already covered under Article 7b EMIR and Article 7 of the draft RTS, adding unnecessary complexity. Supervisors should focus on obtaining clear visibility of the volumes cleared by a counterparty at EU CCPs versus TC CCPs, with an emphasis on gross notional amounts. Market participants should only need to report the number of trades cleared in the relevant subcategories at an EU CCP when subject to the representativeness obligation.

21. **Do you agree with the proposed approach to standardise the reporting arrangements under the active account requirement?**

No comments.

More information

Would you like to respond, or should you have any questions? We would be pleased to hear from you. Please feel welcome to contact Daan Zebel, manager regulatory affairs, dz@dufas.nl Gerwin van de Steeg, manager regulatory affairs a.i., gvds@dufas.nl