Draft CMCE response to ESMA consultation on the clearing obligation for financial counterparties with a limited volume of activity

Last updated: 23 August 2016

Question 1: To which category of counterparties does your organisation belong: (1) in the context of the 1st Commission Delegated Regulation on the clearing obligation, and (2) in the context of the 2nd Commission Delegated Regulation on the clearing obligation?

The Commodity Markets Council Europe (CMCE) is an industry group bringing together commercial market participants active across agriculture and soft commodity, energy, base and precious metals and environmental markets. The group includes commodity producers, merchandisers and consumers, the main commodity trading venues and price reporting agencies. CMCE advocates effective regulation that facilitates the key role of these markets in price discovery and risk management. The majority of CMCE members are non-financial counterparties (NFCs) for the purposes of EMIR. Those members exceeding a clearing threshold (NFC+) will be part of category 4 counterparties for the purpose of EMIR clearing obligation. This applies to both the 1st Commission Delegated Regulation on the clearing obligation of G4 currencies interest swaps and the 2nd Commission Regulation on the clearing obligation for European index CDS.

Question 2: If you offer clearing services, please provide evidence on the constraints that would prevent you from offering clearing services to a wider range of clients.

[Members input required: do relevant CMCE members want to comment?]

Question 3: Have you already established clearing arrangements (1) for interest rate swaps? (2) for credit default swaps? If not, please explain why (including the difficulties that you may be facing in establishing such arrangements) and provide an estimation of the time needed to finalise the arrangements.

The majority of CMCE members are still in the process of investigating clearing arrangements in advance of the 21 December 2018 compliance date of the IRS G4 clearing obligation. Experience to date demonstrates that establishing a clearing arrangement for a NFC can take between 15 and 18 months to implement.

[Members input required: can members provide additional information regarding potential challenges in establishing clearing arrangements by NCFs?]

In this context CMCE members note that the potential constraints that the implementation of the EU harmonised leverage ratio framework under Capital Requirements Regulation (CRR) may have on the availability of the clearing services to small financial counterparties and NFCs. We are concerned that a leverage ratio calibration that does not take account of the risk-reducing effect of cleared derivatives will be the most constraining factor in the availability of clearing services to such counterparties.

[Members input required: do members agree that the implementation of de minimis exemption for small financial counterparties is a solution to advocate? If so, this can be mentioned in this consultation response but the proposed amendment will have to be implemented in the course of EMIR review.]

Question 4: Please provide information and data you may have that could complement this analysis on the level of experience and preparedness of financial counterparties with CCP clearing.

CMCE does not hold this data.

Question 5: Do you agree with the proposal to keep the definitions of the categories of counterparties as they currently are and to postpone the date of application of the clearing obligation for Category 3? If not, which alternative would achieve a better outcome?

In principle, CMCE members do not oppose the proposed two-year delay of clearing obligation for category 3 counterparties as proposed by ESMA. We have consistently advocated for the proportionate application of EU financial services legislation and this solution would be broadly in line with proportionality principle. However, we are of the opinion that the same extension of the clearing obligation should be provided to category 4 counterparties.

Those CMCE members that are NFC+ in great majority qualify for that category by breaching EUR 3 billion threshold for OTC commodity derivatives contracts as prescribed in Article 11(e) of the Commission Delegated Regulation 149/2013. In line with the flawed breach-one-clear-all approach established under EMIR, those counterparties have to develop clearing arrangements for all other classes of OTC derivatives that they engage in and for which the clearing obligation has been determined, regardless of the actual level of their exposure. The only other possibility is to close down their positions in such derivatives altogether, which is likely to adversely impact on their risk-management capabilities. CMCE has advocated changes to this requirement in the context of the upcoming EMIR review.

Should the delay to the clearing obligation for category 3 counterparties be implemented as proposed by ESMA in the current consultation paper, the implementation of clearing obligation for category 4 counterparties would take effect before the obligation will become effective for category 3 counterparties. In particular, the clearing obligation for G4 IRS OTC derivatives would become applicable to category 3 counterparties on 21 June 2019, i.e. six months after the mandate enters into force for category 4 firms. With regards to the clearing obligation in European index CDS, the effective dates would be 09 February 2020 for category 3 and 09 May 2019 for category 4 counterparties. This goes dramatically counter to the principle of proportionality.

CMCE members are of the opinion that given that the rationale for delaying the clearing obligation for category 3 will apply in the same way for category 4 counterparties, there should be an equivalent two year delay for category 4 counterparties. ESMA argumentation summarised in paragraphs 73 -75 of the consultation paper remains equally applicable to small financial counterparties and to NFC+. Cost-effective access to central clearing remains an issue for certain market participants including both small financial counterparties and non-financial counterparties.

Question 6: Do you agree with the proposal to modify the phase-in period applicable to Category 3, by adding two years to the current compliance deadlines?

CMCE agrees with ESMA's proposal but on the condition that the same extension is proposed for category 4 counterparties. Please refer to comments under question 5 for more details.

Question 7: Do you agree with the proposal to modify the three Commission Delegated Regulations on the clearing obligation at the same time?

CMCE agrees with ESMA's proposal but on the condition that the same extension is proposed for category 4 counterparties. Please refer to comments under question 5 for more details.