



**EFAMA**

European Fund and Asset Management Association

# **EFAMA's REPLY TO ESMA's CONSULTATION PAPER ON POST TRADE RISK REDUCTION SERVICES WITH REGARDS TO THE CLEARING OBLIGATION (EMIR Article 85(3a))**

**June 2020**

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EU transparency register: 3373670692-24

# EFAMA's REPLY TO ESMA's CONSULTATION PAPER ON POST TRADE RISK REDUCTION SERVICES WITH REGARDS TO THE CLEARING OBLIGATION (EMIR Article 85 (3a))

## INTRODUCTION

### General comments

- Asset managers and funds are rarely benefiting from post trade risk reduction ("PTRR") techniques, as:
  - o Our volume of transaction by counterparty is below mandatory compression,
  - o Our transactions with each counterparty are directional (i.e. one strategy applies to the entire portfolio), or
  - o Some counterparties are imposing offsetting provisions directly in the master agreement, limiting the right to offset,
  - o Offsetting could cause solidarity between sub-funds, which is illegal under UCITS and AIFMD, even more for multilateral PTRR mechanisms.
- PTRR are risk mitigation tools. Therefore, they should be treated as technical movements in portfolio management and should be exempted from best execution requirements.

**Q1 : Would you agree with the description of the benefits (i.e. reduced risks) derived from PTRR services? Are there any missing? Could PTRR services instead increase any of those risks? Are there any other risks you see involved in using PTRR services?**

We agree with the description provided by ESMA.

PTRR should also be regarded as part of the counterparty risk assessment, as they allow counterparties to assess their counterparties risks by transaction and in a consolidated risk view.

However, entering a portfolio compression exercise or an offsetting of transactions represents an operational risk, e.g. when

- cancelling the right trades and booking a new trade with the appropriate new notional and maturity, or
- calculating the final exposure of the transaction between the counterparties.

**Q2 : Would you agree with this description of portfolio compression? Please explain the different compression services that are offered and how they may differ from the description above. Are there today viable alternatives to using PTRR services to achieve a similar outcome?**

We agree with the definition of portfolio compression provided in §15 - §17 of the CP.

Indeed, compression will result in some derivative transactions to be reduced or terminated and replaced by other transactions with a reduced notional value.

We are not aware of a viable alternative.

The remaining concerns not listed in that description are:

- The requalification of the resulting transaction,
- The notification of the resulting transactions at TR's and eventually CCP's level, and
- The application of the margining mechanisms.

**Q4 : Should there be a clearing exemption for PTRR trades that are a direct result from a portfolio compression? If not, why? Is there a difference between bilateral and multilateral portfolio compression for the sake of an exemption?**

We are in favour of a clearing exemption for all PTRR trades that are a direct result from a portfolio compression, as PTRR are risk mitigation tools.

**Q5 : Would you agree with this description of PTRR Services? What other forms of PTRR services exist? What do they do? How do they work? Are there any other viable alternatives to PTRR services, if yes, why are they not sufficient?**

Even though we do not see the benefit of such mechanisms from a risk management's perspective, we agree with the definition of the PTRR services provided in §18 – §20 of the CP.

**Q9 : Should there be an exemption from the clearing obligation for PTRR trades (other than portfolio compression) that are a direct result from a PTRR exercise? If not, why?**

In line with our reply to Q4, we are in favour of a clearing exemption for PTRR trades (other than portfolio compression) that are a direct result from a PTRR exercise, as PTRR are risk mitigation tools.

**Q17 : Do you think an exemption from the clearing obligation is not needed for legacy portfolios and PTRR services generally? To what extent can the use of plain vanilla transactions in PTRR services be replaced with the use of non-plain vanilla transactions, or should this be avoided? Please explain.**

They should benefit from the same exemption as other equivalent transactions.

**Q18 : Would an exemption to the clearing obligation contradict the G20 commitments? Please explain.**

We do not consider an exemption to the clearing obligation as a contradiction to the G20 commitments, which are aimed at mitigating the systemic risk. As a risk reduction tool, PTRR do not create systemic risk concerns.

**Q19 : How could an exemption to the clearing obligation for PTRR trades lead to a circumvention of the clearing obligation? Please explain.**

Please refer to the systemic risk aspects covered in question 16.

**Q20 : Would you consider introducing an exemption to the clearing obligation as an incentive not to clear transactions that technically are covered by the clearing obligation. If yes, why?**

The use of PTRR should not be considered as an incentive not to clear OTC derivatives transactions.

Their characteristics are very distinct, and they should rather be considered as tools that improve:

- the accuracy of the counterparty risk management, and
- the collateral liquidity management.

**Q21 : Are there risks with reducing collateral? Even if complying with regulatory requirements, could this lead to such capital being used to increase risks, possibly systemic risks?**

If the offsetting and compression are calculated before the movement of collateral, any subsequent reduction of collateral would be negligible.

In our view, the reduction of collateral does not increase systemic risks, but rather avoids a risk of over-collateralisation.

**Q23 : Should conditions, similar to the ones as outlined above, apply to a possible exemption under EMIR for PTRR transactions? Should other conditions apply? Would the answer depend on the type of PTRR service? Please explain.**

We urge ESMA and the European Commission to ensure that any change to the EMIR Refit does not endanger existing recognitions of equivalence.

**Q27 : To benefit from an exemption to the clearing obligation, to what extent should parties to a PTRR exercise be able to be changed, i.e. not limited to the original counterparties? Would the answer depend on the type of PTRR service? Please explain.**

To guarantee sufficient control of counterparty risk, the counterparties should remain the same.

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