

HYBRID TRANSACTION REPORTING MECHANISM

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INTRODUCTION

ESMA's consultation dated March 26, 2020 (ESMA74-362-47, "CP") describes a clear extension of data fields to be reported by market participants in accordance with Art. 9 EMIR. Taking into account that EMIR currently requires a dual-sided reporting, our members have discussed how the relevant objectives can be reached while lowering the burden falling upon economic operators and citizens.

To achieve this, we believe that a Hybrid Transaction Reporting Mechanism ("HTRM") should be considered. Under the HTRM approach, one party (sell-side) will report all data fields while its counterparty only reports a subset of data fields. Besides, a closer involvement of ANNA DSB may further increase the relief provided by HTRM as an add-on.

Introducing the HTRM approach is necessary to comply with the principle of proportionality. It would also strengthen European financial markets which are competing on a global scale. HTRM would enable a fair compromise between the known transaction reporting systems (single-sided / dual-sided).

This paper aims to provide a coherent description of the HTRM approach.

I. PRINCIPLE OF PROPORTIONALITY¹

According to Art. 5 para. 1 and 4 of The Treaty on European Union, the use of Union competences is governed by the principle of proportionality. For European institutions Protocol No 2 further clarifies the application of the principle of proportionality.

Draft legislative acts, which include proposals from the COM (Art. 3 of Protocol 2) shall take account of the need for any burden falling upon [...] economic operators and citizens, to be minimised and commensurate with the objective to be achieved (Art. 5 of Protocol 2).

HTRM, as further specified below and already suggested by EFAMA in response to ESMA's consultation dated March 26, 2020 (ESMA74-362-47, "CP"), aims to reduce the intended burden on economic operators and citizens without conflicting with the objectives to be achieved with ESMA's draft Technical Standards.

II. OBJECTIVES OF THE DRAFT TECHNICAL STANDARDS

With respect to reporting all details regarding derivative contracts it has been the overarching goal at Level 1, to make **information on the risks inherent in derivatives markets** centrally stored and easily accessible, inter alia, to ESMA, the relevant national competent authorities, the European Systemic Risk Board (ESRB) and the relevant central banks of the ESCB (Recital 41 of Regulation (EU) No 648/2012). A **comprehensive overview of the market** and the **assessment of systemic risk** is aimed (Recital 43 of Regulation (EU) No 648/2012).

The current draft Technical Standards aim to **enhance the quality** of the reported derivatives data (Page 10 CP).

Further, ESMA intends to align the reporting requirements in the EU with the global guidance on **harmonisation of OTC derivatives data elements reported** to TRs, as developed by the CPMI and IOSCO working group for the harmonisation of key OTC derivatives data elements (Page 10 CP).

¹ All provisions referred to are included in Annex 1.

III. HYBRID TRANSACTION REPORTING MECHANISM

1. Basis

First, we would like to point out that references made to the principle of proportionality are not meant to put in question the work done on the draft Technical Standards. We believe that ESMA has created it diligently, especially considering the complexity of this matter.

Furthermore, level 1 requires a dual-sided reporting. It is not aimed to request a single-sided reporting by referring to a HTRM.

However, the principle of proportionality requires to consider a more hybrid transaction reporting mechanism. ESMA describes in margin note 265 of the CP with regards to data elements related to collateral, margins, and counterparty rating triggers:

“ESMA proposed to keep this field in place. The current format provides sufficient information under a dual-sided reporting regime, but it is not compatible with information gathered under a single-sided regime. Therefore, in order to facilitate global aggregation of derivatives information, ESMA proposes, to extend the categories that need to be reported in this field in order to capture the collateralisation by both counterparties to the transaction.”

In other words, if additional categories are reported by at least one of the counterparties, it would provide ESMA with sufficient information.

If receiving information from one counterparty would be sufficient to enhancing the data quality while harmonising data reporting fields, there should be a broader consideration of this hybrid transaction reporting structure. This would minimise the burden falling upon economic operators and citizens and would still be commensurate with the objective to be achieved. Dual-sided reporting should only be considered as far as required for achieving the objectives of EMIR and its Technical Standards.

2. Who shall report all data fields?

Prior to focussing on the data fields that should be reported by only one of the counterparties, it is important to be clear as to who shall be obliged to report the full set of data fields. Asking the sell side with regards to uncleared OTC derivatives and Central Counterparties in all other cases for reporting the full set of data would mean a huge relief for financial market participants (including UCITS and AIFs) while improving the data quality.

a) Uncleared OTC-Derivatives

With respect to uncleared OTC-derivatives, we believe that it should be the sell side who should report all data fields. Since the notion of “sell-side” is not legally defined, we believe it would be appropriate to define it by including (i) credit institutions, who are authorised in accordance with Directive 2006/48/EC (each a “**Credit Institution**”) as well as (ii) “Authorised Reporting Counterparties”. An “**Authorised Reporting Counterparty**” (also “**ARC**”) means any other person who has registered with ESMA as such and has concluded or aims to conclude an OTC-derivative with a counterparty seated in the European Union. Registering as ARC shall come along with the obligation to report under Art. 9 EMIR as if the ARC was a Credit Institution (that means, the full set of data fields is to be reported).

It is part of the business model of many Credit Institutions to become counterparty of derivatives for clients from any other sector. Against this background it is often the case that at least one of the counterparties is a Credit Institution.

Allowing other market participants to become obliged under Art. 9 EMIR as if they were Credit Institutions creates a level playing field for the sell side. Limiting HTRM to OTC-derivatives with Credit Institutions would otherwise set an incentive to conclude OTC-derivatives with Credit Institutions only. This would in particular hamper market participants from third countries to access European OTC derivative markets. We believe that only sell-side market participants who are not Credit Institutions would make use of the possibility of registering as ARC. Introducing such voluntary registration as ARC would also increase the number of dual-sided reports under Art. 9 EMIR.

b) Cleared OTC-Derivatives and Exchange Traded Derivatives

With regards to cleared OTC-Derivatives and Exchange Traded Derivatives only Central Counterparties shall be obliged to report the full set of data. This would mean the same direction as the current Commission demand for a single sided-reporting regarding ETD² While a single sided reporting would require an amendment at level 1, considering the HTRM approach is possible without amending level 1. Market participants would not be required to implement the new data fields while facing the uncertainty of a later amendment of level 1 regarding ETD, of course depending on the concrete data fields that will be declared subject to the HTRM approach.

We believe that data which originate from Central Counterparties are most reliable and should be treated as such.

3. Which data fields shall be made subject to HTRM?

Taking into account the new data fields which have been proposed by ESMA, Q 26, 71, 87, 94, 98 and 108 of the CP refer to fields, which can be considered as examples of fields that can be made subject to HTRM without failing to achieve the objectives.

The following example (Q94) illustrates this principle:

Baskets (as underlying) include numerous components with different weightings. Especially the diversification which is inherent to baskets makes it difficult to understand why further data regarding the constituents is requested. Diversification of components make them have a much lower impact on markets than physical investments or derivatives which are only referencing one component. Against this background one may have concerns that requiring all market participants to implement these additional fields for derivatives on baskets would be necessary to obtain a comprehensive overview of the market and to assess systemic risk (Recital 43 of Regulation (EU) No 648/2012). At least these fields are required to be collected from both counterparties of a transaction.

The above provides a concrete example. However, ESMA and the NCAs are best placed to identify the data fields that have been most valuable for their work since the introduction of EMIR and which fields are crucial for their work. Therefore, ESMA should assess which fields can be made subject to HTRM to minimise the burden falling upon economic operators and citizens while remaining commensurate with the objective to be achieved.

² <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2017%3A208%3AFIN> (page 10, Art. 7b (a)).

IV. CLOSER INVOLVEMENT OF ANNA DSB

Discussing alternatives making the reporting requirements a smaller burden falling upon economic operators and citizens while still commensurate with the objective to be achieved, could also mean a closer involvement of ANNA DSB.

The sell-side, including Credit Institutions³ could be mandated to provide all required ESMA reference data fields to ANNA-DSB when they aim to use (OTC) ISIN for all derivative products subject to the EMIR reporting obligation. This requirement should not be restricted to TOTV-ISINs according to MiFIR. At the same time ESMA, NCAs and TRs must be requested to obtain such data only from ANNA-DSB going forward. Thereafter they need to enrich the individual transaction messages themselves as needed.

ESMA should not have any political issues with ANNA-DSB as central reference data base for derivative instruments. The EU/ESMA had been instrumental in the set-up of ANNA-DSB and are following the FSB approval of ANNA-DSB as global UPI provider. Also, global regulatory community acceptance is given. With such a solution the size and complexity of the existing EMIR transaction reports from counterparties to the trade repositories could be reduced to a minimum. Reporting would be more efficient and secure. Duplication of databases and data reconciliation efforts along the reporting chain could be avoided if ANNA-DSB is appointed as the golden source of issuer supplied derivative instrument reference and necessary flow data for all EMIR transaction reporting. ANNA-DSB seems to be ready for such an approach. Their response⁴ to the CP includes the following lines:

“Last but not least, the DSB notes that the consultation paper contains an increase in the number of data elements to be stored and/or reported by market participants. Should regulators and practitioners find it helpful for a centralised data source to be utilised to assist with the creation and distribution of the static data elements, the DSB stands ready to assist by facilitating discussions on the subject of whether and how these values could be centrally generated, in an effort to assist with enabling greater consistency, improved data alignment and transparency.”

The closer involvement of ANNA DSB can also be considered as add-on to HTRM. The two approaches can be combined and do not conflict with one another.

³ Please see IV. for the definitions.

⁴ <https://www.esma.europa.eu/file/56166/download?token=u-2zNV6r>.