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FIA Europe EMIR Trade Reporting Working Group:

"Reporting Valuation and Collateral Data under EMIR for 12 August 2014"

July 2014

Table of Contents

1. Purpose of this document

The purpose of this document is to represent the views of the exchange-traded derivatives industry with regard to the reporting of valuations and collateral data under EMIR[1].

1.1. Background

Since early 2013, FIA Europe has been working with members to interpret EMIR's reporting requirements for exchange-trade derivatives (ETDs). A significant degree of analysis and consensus building has been required amongst market participants to develop an agreed interpretation of EMIR's reporting rules. Following the initial reporting start date of 12 February 2014, we have turned our attention to the reporting of collateral and valuation data under EMIR, for which the reporting start date is extended by 180 days after 12 February 2014, to 12 August 2014.

We have engaged with ESMA staff and national competent authorities to discuss how best to apply the collateral and valuation rules to ETD markets, to ensure both alignment with EMIR's objectives and a consistent interpretation across market participants.

We are grateful to ESMA staff and to the national competent authorities for publishing the 23 June 2014 "Questions and Answers" document (Q&A), which included useful guidance on collateral and valuation reporting[2]. We have commented on the relevant Q&A sections below, adding our interpretation and intended approach.

As noted, ESMA's guidance in this form to the industry has been of critical importance, since the technical standards had not been crafted for ETD market mechanics. For example, the following characteristics of the ETD market are not reflected in EMIR's reporting rules, leading to the need for interpretation and an agreed reporting approach:

- the varying clearing and operational processes across the different CCPs in Europe (22 CCP members of EACH[3] operating in 16 countries)
- variability in the end-to-end trade and clearing process for ETD business
- that 'netting' of individual trades is a core process and that the original trade level data is not subsequently held by all CCPs
- that different market participants have access to different degrees of information, depending on their role

This document seeks to share the outputs of FIA Europe's Working Group as part of a collaborative approach to developing an industry response. The collateral and valuation fields (17 to 26 of Table 1) are considered "Counterparty Data" under EMIR's Implementing Regulation (EU) No 1247/2012

[1] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories.

[2] The most recent version of ESMA's document is "Questions and Answers on Implementation of EMIR, 10 July 2014/ESMA/815, available at http://www.esma.europa.eu/news/ESMA-publishes-10th-updated-EMIR-QA?t=326&o=home.

[3] European Association of CCP Clearing Houses. See www.eachorg.com

(“ITS on TR Reporting”). While Counterparty Data does not require prior agreement between the parties before reporting (as with “Common Data” in Table 2), it is clear that a consistent interpretation of the rules is required to ensure the data reported is meaningful and meets the objectives of the legislation.

2. When the obligation starts

2.1. Timing for reporting

ESMA’s Q&A states on page 61 that the “reporting start date is extended by 180 days for the reporting of information referred to in Article 3 of Regulation (EU) 148/2013, i.e. data on exposure. The corresponding fields in the table are the fields related to valuation and collateral…The resulting date is therefore 11 August 2014 with the first reports being due no later than the end of 12 August 2014 including the valuations and collateral as at the end of 11 August 2014.”

3. Principles

We applied a number of key principles to our interpretive work:

- For data quality purposes, the data fields should be interpreted consistently by ETD market participants, in spite of the fact that the data fields are in the Counterparty Data table (and not required to ‘match’ under the legislation

- A consistent interpretive approach should be applied between asset classes and with OTC, for the sake of simplicity and to minimise the need for different sets of ‘logic’

4. High level approach

We developed the following high level approach:

- Reporting of valuation and collateral data will be at the position level, provided that all the conditions are met under TR Answer 17 in the ESMA Q&A with respect to the reporting of the respective trade level data.

- Given that reporting collateral at a portfolio level is permitted further to Article 3 of Commission Delegated Regulation (EU) No 148/2013, we infer that a portfolio of collateral can be reported against multiple positions and/or across accounts. This is supported by TR Answer 3a(a5), which states that “the collateral reported should be just the collateral that covers the exposure related to the reports made under EMIR. If it is impossible to distinguish within a pool of collateral the amount which relates to derivatives reportable under EMIR from the amount which relates to the other transactions the collateral reported can be the actual collateral posted covering a wider set of transactions.”

- ESMA’s TR Answer 3b indicates that the contract valuation should be “reported on a daily basis at position level, as maintained and valued by the CCP”. We believe that a consistent valuation methodology should be used by all market participants (clearing members, CCPs and clients) and with respect to both ETDs and the OTC market (the valuation method for ETDs should be aligned with the ‘net present value’ approach for OTC derivatives contracts (see the para below – ‘Report cumulative variation margin)

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5. Mark to Market approach

5.1. Field 17 – Mark to market value of contract

Field 17 of Table 1 Counterparty Data is to be populated with the "Mark to market value of the contract". Article 3(5) of the RTS on Reporting to a TR sets out that "for contracts cleared by a CCP, mark to market valuations shall only be provided by the CCP". Further, ESMA's Q&A[4] states that for "transactions cleared by a CCP, fields on the contract valuation should be reported on a daily basis at position level, as maintained and valued by the CCP. This does not mean that the report should be made by the CCP. The CCP may make data available to counterparties so that the latter report. The use of CCP valuation data does not mean duplication of reporting."

Participants in ETD markets employ a number of different valuation methodologies for trades and positions. It is therefore important to agree on a consistent methodology for use by CCPs to ensure that mark to market values are meaningful and enable regulators to meet their objectives.

Report cumulative variation margin
We conclude that the best approach is to report the cumulative variation margin, which is akin to net present value with respect to OTC derivatives. We do not believe the alternative, which is to report the daily variation margin, makes sense. Cumulative variation margin measures the difference between the original open trade price and published end-of-day current settlement price, to reflect the unrealised profit or loss. The market value at position level is calculated using the current settlement price and the original open trade price. Clearing members and clients typically use this method for valuing ETD positions. The value reported will be with respect to the position only (and not the trade), in alignment with the guidance in ESMA Q&A TR Answer 17.

Alternatively, reporting the daily variation margin for positions would only measure the difference between the previous day's settlement price and the current settlement price. This would show the daily movement of risk, using published end-of-day prices at a position level. This would only capture the day-on-day change in market price and position.

5.2. Field 18 – Currency of mark to market value of the contract

Field 18 is to be populated with the "currency of mark to market value of contract" as defined in the exchange contract specification

5.3. Field 19 – Valuation Date, and Field 20 – Valuation Time

EMIR's technical standards allow some room for interpretation in terms of how to populate the valuation date and time. We have taken a pragmatic approach, given that all ETD trades, regardless of the exchange or CCP involved, are valued on a daily basis.

Report date as prior business date
Determining the valuation date is relatively straightforward – we have determined that the prior business date will be populated in this Field. This is because the settlement prices taken from the prior business day will have been used to report on T+1.

Report time as "23:59:00 UTC"
In terms of valuation time, one option is for each reporting firm to use its 'batch processing time'. While this is a simple implementation, each counterparty would have its own internal time stamp for the batch processing time, meaning no possibility of a match with one's counterparty, and we question the value of an internal batch time for regulators. The other option is to use the dates and times

[4] Questions and Answers on Implementation of EMIR, 10 July 2014/ESMA/815. TR Answer 3b(a), p.61.

published with the settlement prices by the respective exchange or CCP. This requires a relatively complex technical build to add an external data feed from the exchange or CCP to the reporting firm. This will also require firms to consume external data before reporting can be done. The benefits of this build are unclear, given that the prices are published once daily by all CCPs/exchanges, albeit at different times by each, based on their own internal processes.

For the reasons above, we determined that the best approach is to use a generic time of "23:59:00 UTC" for the valuation time for ETDs. This will result in time stamps being consistent across all CCPs reports as well, provided this approach is follows by all ETD market participants.

5.4. Field 21 – Valuation type

Field 21 provides two options: "M = mark to market / O = mark to model.

ESMA's Q&A TR 3(b)(c) on page 62 states that "whenever a price is available for the valuation, such valuation should be considered as 'mark-to-market". This aligns with our view that the valuation type will always be 'M' for ETDs, because clearing members and their clients will use the market price set by the exchanges/CCPs. Rarely will it be the case - in the context of ETD markets - that clearing members or clients will exercise significant subjective judgment in transforming market inputs into the final value of a position. Where a valuation involves significant subjective judgment and assumptions, this would fall into the category of a mark-to-model valuation, in our view. This is not the case with respect to ETD valuations.

6. Collateral approach

6.1. Field 22 – Collateralisation

Field 22 in 'Table 1' Counterparty Data asks whether collateralisation was performed, with the following format to be used:

U = uncollateralised
PC = partially collateralised
OC = one way collateralised or
FC = fully collateralised

ESMA's Q&A TR 33 on page 78 introduces definitions for the above terms, which we welcome.

Report "Uncollateralised" re clients, and "One Way" versus CCPs

Following the guidance in ESMA's Q&A TR33, our approach with respect to reporting with a client as counterparty will be to report "Uncollateralised" in field 22, because we do not as clearing members post collateral to our clients. When, however, a client has **delegated** its EMIR reporting to its clearing member, the clearing member will report, on the client's behalf, that collateral has been posted "One Way" (posted to the clearing member by the client).

With respect to reporting with a CCP as counterparty, clearing members will report "One Way", to indicate that the clearing member has posted collateral to the CCP. We would expect CCPs to similarly take the approach that they do not post collateral to clearing members, and hence to report "Uncollateralised" when reporting against clearing members.

6.2. Field 23 – Collateral Portfolio

Field 23 in Table 1 asks whether collateralisation was performed on a portfolio basis (Y = Yes or N = No). For ETDs, the answer will always be "Y". We note ESMA's Q&A, TR Answer 3a (a) which says on page 60, "the reporting of each single executed transaction should not include all the fields related to collateral, to the extent that each single transaction is assigned to a specific portfolio and the relevant information on the portfolio is reported on a daily basis (end of day)."

6.3. Field 24 – Collateral Portfolio Code

Field 24 in 'Table 1' is to be populated with "Up to 10 numerical digits" for the collateral portfolio code.

There are two problems here:

- The requirement to use only 10 digits is too restrictive – at least 20 characters are needed
- Most firms use alphanumeric formats and other symbols/hyphens to name portfolios

Our approach, given this problem, is to recommend that firms obtain guidance from their trade repository or third party reporting service with respect to what will be accepted for Field 24. We believe a change to the Implementing Technical Standards (ITS) is necessary to make Field 24 less restrictive. We understand that ESMA and national competent authorities are aware of this issue.

6.4. Field 25 - Value of the collateral

Field 25 in Table 1 describes the "Value of the collateral" as follows: "Specify the value [of] the total amount of collateral posted".

We welcome ESMA's Q&A TR 3a which clarified to some degree what should be included in the calculation of the total amount of the collateral.

Non-settled or "in-flight" collateral:
The term "posted" in Field 25 is not defined in the legislation, so prior to ESMA's recent Q&A comments, it was unclear how to treat collateral which the "poster" intends to post, but which the receiver has not yet received.

ESMA's recent Q&A TR 3a(a6) states "the collateral should be reported as the total market value that has been posted by the counterparty responsible for the report. The fact that certain types of collateral might take a couple of days to reach the other counterparty should be ignored."

We welcome this guidance. We will point out however that in cases where a clearing member is reporting on behalf of a client in a **delegated reporting** scenario, the clearing member will be, on the client's behalf, reporting the value of the collateral posted to the clearing member. There are currently different practices among FIA Europe's clearing firms regarding the treatment of cash and non-cash collateral sent to the clearing member by its clients. Most clearing firms currently treat "in-flight" cash collateral from clients differently from in-flight non-cash collateral. For example, a number of firms will take into account any in-flight ***cash*** collateral from a client when calculating the daily margin requirement, but not the in-flight non-cash collateral, which will only be "booked" when settled. Other clearing members will not include any unsettled collateral, cash or non-cash, when calculating the client's margin requirement. It may as a consequence be the case that the reporting date of a portfolio and the actual settlement of the associated collateral will differ.

Include IM, VM and other balances:
ESMA's Q&A TR Answer 3(a)(a4) on what to include in the collateral calculation is aligned with our conclusion on the best approach here. We will include in Field 25 both initial and variation margin, along with any other balance types held as part of the cash balance at the end of day, plus any securities on deposit at market value, not adjusted for any haircut by the CCP. For the avoidance of doubt, the value of the collateral will include open trade equity, cash balance and non-cash collateral.

Report pre-haircut value of the collateral:
ESMA's Q&A TR Answer 3a(a) states "the collateral should be reported at the total market value that has been posted by the Counterparty responsible for the report. Therefore any haircuts or similar used by the receiver of the collateral and any fees or similar amounts should all be ignored."

We reached a similar conclusion. When considering the non-cash component of collateral, we determined to not apply a haircut to the collateral value. A haircut (a reduction of the value of the assets) is applied by the *receiver* of collateral, not the entity posting the collateral. Thus, when reporting with a CCP as the counterparty, the clearing member will report the value of collateral on a pre-haircut basis. We add that receivers of collateral may in fact apply different haircuts to the same security, which bolsters the argument for pre-haircut reporting.

As noted above, we will populate the "Collateralisation" Field 22 with a "U" when our counterparty is a client, since we do not post collateral to our clients. Consequently, when a client is our counterparty the value of collateral in Field 25 will be left blank or not reported, depending upon which trade repository the firm is using.

However, when reporting on behalf of a client in a **delegated reporting** scenario, we will report a value of the collateral, as noted above, but we will not apply a haircut to the value reported, in line with ESMA's Q&A TR Answer 3a(a), and for the sake of consistency with the approach taken with respect to reporting with CCPs as counterparty.

6.5. Field 26 – Currency of the Collateral

ESMA's Q&A TR Answer 3a(a2) states "all collateral for a single portfolio should be reported in one single currency value. The reporting counterparty is free to decide which currency should be used as a base currency as long as the base currency chosen is one of the major currencies which represents the greatest weight in the pool and is used consistently for the purpose of collateral reporting for a given portfolio."

We had discussed how to represent a multiple currency portfolio, which includes both cash and non-cash assets, and so we welcome the clarity provided in the Q&A noted above. We will undertake aggregate, single currency reporting and not report 'asset by asset' in a multiple line or multiple currency approach for field 25 (i.e. values for 25a, 25b, 25c). While this will not provide transparency regarding the components of collateral received, or the prices / foreign exchange rates applied, but it will be easier for regulators to compare collateral values across trade repositories.

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Annex 1: Definitions and worked examples

Annex 2: FIA Europe EMIR Trade Reporting Working Group

The group is comprised of 11 clearing members:

Members of working group
Goldman Sachs (Chair)
Barclays
Citi
Credit Suisse
Deutsche Bank
HSBC
JP Morgan
Morgan Stanley
Nomura
UBS
Soc Gen Newedge