

EMIR Implementation: Segregation & Portability

Meeting with NCAs

September 24th 2013

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EMIR Implementation Timetable – phased compliance

The issues raised impact both existing ETD and future OTC cleared products

Proposed Implementation Timetable

By end of April 2014:

- Full separation of House and Client positions
- All Clients in a minimum of an EMIR compliant Omnibus Account for EU CCP business
- All Clients in receipt of applicable EMIR disclosures and terms of business addenda

By end of 2014:

- Completion of scalable technology build across Accounting/Banking/Treasury/Clearing/Reporting to support individual segregated accounts within the constraints of available CCP infrastructure

By end of Q1 2015:

- On-boarded all clients who have requested individually segregated accounts subject to constraints and validity of take-up estimate

EMIR Implementation Timetable – phased compliance proposals

Key Dependencies/challenges:

1. CCPs must be able to offer clearing members the necessary account structures to accommodate affiliate and/or TTCA client account requirements – this would include provision of multiple omnibus accounts to facilitate separation of proprietary affiliate and client business with the ability to meet margin calls in separate transactions from different sets of bank accounts.
2. In order for CMs to leverage CCPs' own disclosure documentation for their own client communication, CCP disclosures must be client-friendly and accessible by clearing members as soon as possible.
3. Functional specification from CCP must offer the clearing member automation to facilitate efficient treasury and collateral movements and hence maintain high levels of STP (one CCP is asking members to make excess declarations via fax).
4. CCPs must be able to support an unlimited number of ISAs per clearing member irrespective of product class from go-live.
5. Where a CCP has a dependency on separate PPS accounts per client, the applicable payment banks must have the ability to support the increased demands this will place upon them (PPS banks have expressed their concerns in this area).

EMIR Segregation/Portability: Outstanding questions

The following list reflects the feedback from clearing members only

Excess Management within an ISA:

1. ESMA Q&As defined excess as the difference between IM called by the CCP and the IM called by the CM – are clearing members permitted to allow a client to maintain an excess balance on an ISA generated by a VM credit, or option premium or fall in IM requirement (due to reduced positions)?
2. If a client posts collateral to the CM to cover any future IM liabilities across a combination of its omnibus and/or ISA accounts or any non-EU CCP liabilities, when/how should this be treated as EMIR mandatory excess?
3. Where a client has posted margin (this could be FX equivalent to the currency posted to the CCP) to the CM after the relevant 'cut-off' time, how should this margin be treated and managed?

Segregation obligations for clearing members

1. FCA has stated that the segregation obligations apply to any EU CCP clearing member including US FCMs. Given that US FCM clearing members are obliged to comply with CFTC Part 30.7, 4d (a) and 4d(f) of the CEA, how should firms manage the inherent conflict between these requirements?
2. Position allocation – when an order has been executed and the resulting trade is awaiting allocation to the client's end account at the CM or give up clearing firm, the position is currently held at the CCP within the House or Client pending or 'default' account (depending on CCP) – is there any expectation that this should change?
3. Would it be possible for a clearing member to open an ISA in the name of a fund manager as opposed to the names of the underlying funds?

EMIR Segregation/Portability: Outstanding questions

Client Disclosures:

1. In respect of client disclosures around the different levels of segregation and associated protections, the FOA is currently drafting a standard industry document which will include a generic disclosure, comparative analysis of the different segregation models across CCPs and then reference CCPs' own disclosure documentation.
Would the NCAs be willing to work with the FOA in the production of a compliant disclosure document?
2. In respect of a disclosure on costs/fees – currently FOA is very reluctant to discuss any common approach to this obligation even in terms of the development of a standard template due to competition law concerns.
Do the NCAs believe that it would be possible and viable for the industry to agree a standard template for such a disclosure – one which sets out a set of standard criteria which firms use to determine fee rates and a set of standard discount metrics (firms would then select the criteria and metrics that their firm applies)?

CCP Application Process

1. Will ESMA or applicable regulators provide a greater level of transparency around CCP applications now that the statutory deadline has passed?
 - CMs would like to know if a CCP application has been materially amended as a result of the review carried out by the relevant NCA/College?
 - CMs would like to know whether a CCP application is going to be approved before the statutory 6 month time limit?
 - CMs would like to know which CCPs have applied for authorisation (FOA has been informed that Weiner Borse has not applied despite their stated intention to do so).

CASS/Client Money Issues

1. Individual Seg Accounts operate under different legal and operational constructs at different CCPs. This makes it impossible for Clearing Members to establish a consistent flow.
 - Most CCPs intend to 'bulk up' PPS cash transactions for ISAs into a single cash movement irrespective of how the client has contracted with the CM ie CASS or TTCA
 - It is not clear whether all CCPs can break out payment for TTCA and CASS omnibus accounts
2. There appears to be a lack of clarity for cash in transit between the CM and CCP where clients operate in different regulatory protection regimes e.g. a combination TTCA and CASS or for non-EU markets. This may lead to:
 - Clients may be required to use different cash flows to pay margin to the same broker entity – one for CASS and one for ISA. This will increase the incidence of operational errors
 - Clients may not be able to accommodate multiple payment flows leading clients to opt out of CASS protection
3. There is a lack of clarity as to whether an ISA account is excluded from the CASS client money calculation. It is assumed an ISA is not part of a primary pooling event. In the event that an ISA is included in the CASS client money calculation, there is a potential increase in double segregation which could push clients to opt out of CASS protection.
4. There is a lack of clarity as to whether trust letters are required for ISA accounts. If they are, this will lead to a proliferation of trust letters and a delay to the account set up due to proposed changes in CP 13/05 to remove the 20 day grace period. Further, what recourse is available in the event that a CCP does not sign a trust letter?

ISA Take-Up Assumptions

During the 5th September meeting, the FOA was asked to provide additional detail underlying the assumptions regarding ISA take-up – specifically to provide further detail across client types.


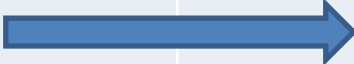




In response to this request, clearing members said that client take-up will be determined by a range of factors including:

- / Cost of service provision by CCP
- / Cost of clearing member service provision – IT, banking, staffing etc.,
- / Capital efficiencies for clients subject to Basel III
- / Product and risk exposure for the client
- / Operational burden and overhead for the client
- / Fund mandates of asset managers

As there are very significant uncertainties across all these factors, clearing members are unable to provide any additional detail as to the take-up assumptions. These were as follows as per the 5th September presentation:

- *Each major CM has on average 4 to 5 large asset management clients, with each asset manager charged with controlling 100 to 150 funds that will require separate account. Assuming a median 125 funds, this results in 125 fund accounts per manager and means that each CM will have up to 600 accounts under administration for their asset management clients alone.*
- *This does not include the remaining spectrum of the client base; Funds (Hedge, Pension, Sovereign Wealth) along with HNW client, which on average will result in an additional 400 accounts to administer.*
- *This assumption can be viewed as conservative and at the lower end of client account numbers that FOA members provided as part of this analysis.*

Standard CCP Roadmap/Timeline for major CCP Clearing System change

CCP System release	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6	Month 7	Month 8
Release of information: High level timeline and Preliminary Technical Release Notes (members/vendors)								
Impact analysis: member and client consultation Period								
Final Release of Info: Business and tech and Schedule								
Simulation /Test Environment available : For development and testing								
Conformance Testing: UAT, DR and member readiness								
Final Deployment Roadmap								
Go-Live								