

EMIR Article 39 IMPLEMENTATION CHALLENGES

Meeting with the FCA/BoE/Bundesbank/BaFin

Summary note

The FOA/ISDA and a group of practitioners met the FCA/BoE/Bundesbank/BaFin on Friday 1st November as a follow up to our meeting with the NCAs on 24th September on EMIR Implementation.

The NCA attendees were as follows:

Helen Boyd - FCA

Barry King - FCA

Heather Pilley – FCA

Victoria Cooley - FCA

Emad Aladhal – FCA

Ben Mitchell – BoE

Andrew Powell - BoE

Anna Pliquett – Bundesbank

Christian Weiss – BaFin

The main take-aways were as follows:

1. Clearing member technology build roadmap

Following the meeting we held with the NCAs on 24th Sept, where we presented a number of proposed timelines including that clearing members would need until the end of 2014 to complete the build of a scalable individual segregation systems infrastructure across all EU CCPs, we were asked to provide a greater level of granularity around this timeline so that the regulators could get a better understanding of the build requirements and what parts of this could be done once and what would need to be built for each CCP separately. To this end, we presented the attached slides (ISA Build Roadmap). In response, the FCA made the following observations:

- (i) In response to a dialogue around vendor readiness, the FCA said that they were disappointed that firms/vendors hadn't made more progress towards building to those ind. seg. models which have been offered by CCPs for some time (e.g Eurex, NOMX). We flagged that one of the major vendors was requiring all clients to upgrade to the latest software version in order to benefit from EMIR functionality – normally such an upgrade will be considered a major project for firms.
- (ii) They asked about the extent to which testing could be done in parallel across CCPs and which elements of IT development could be prioritised. We pointed out that EMIR development has to be resourced against a background of a number of other demands, including algo tagging, migrations to other clearing platforms (e.g LIFFE to ICE), Eurex Prisma, EMIR TR reporting etc...
- (iii) The FCA asked whether firms could develop a tactical solution for ind seg for 'day one'. The response was that this was possible but entirely dependent upon the number of clients for whom this would have to be developed, the number of CCPs involved, and how significant the banking/treasury bottlenecks will be. We also highlighted again the operational risk involved in operating so-called 'tactical' solutions for more than a minimal number of clients.

- (iv) In a discussion around client outreach and the extent to which clients are engaging with firms, it was clear that v few firms have started anything formal yet although one firm that had, noted that clients were demanding a significant level of 'hand holding' to explain terms of business addenda etc.. This would suggest that it is going to take a considerable time for clients to give their written choice of seg model and agree to ToB addenda. FCA said that they are still discussing how firms should deal with the situation where clients do not reply on a timely basis but they will take comfort from the fact that clients will, at a minimum, be in an EMIR-compliant net omnibus account separate from House.

2. CCP Information gaps

The FOA was asked by FCA to update them on what information (regarding the implementation of their planned segregation models) had been forthcoming from CCPs to date. The FCA commented that our summary was consistent with the feedback they had received. They said that they were aware that much of the information had been made available via bilateral meetings with clearing members although some CCPs had started holding seminars with firms through which such information was being disseminated. The FCA stressed again that clearing members must urge CCPs to provide them with all the information they require and should not expect regulators to do this for them.

3. Clearing member compliance timeline

The FCA made it v clear that there is no scope whatsoever for any extension to the compliance deadlines associated with offering a choice of segregation models to clients – these are driven by the Level 1 legislation which is not going to change (please note that the procedure whereby ESMA recommended a change (an extension) to the implementing technical standards regarding TR reporting for ETD is NOT available to them in respect of Article 39 as there are no such technical standards underlying this Article). The FCA stressed that this issue had been discussed with other EU NCAs and at the ESMA Post Trade Standing Committee.

The FCA then went on to say that they wanted to invite all UK firms who are clearing members with EU clients of any EU clearing house to contact the FCA before November 15 to schedule a bilateral meeting with them to discuss their implementation of the Segregation and Portability arrangements required under Article 39 of EMIR. Their focus will be on EMIR Art 39 (also Art 38, if necessary), but not on other provisions of EMIR. In particular, the FCA wish to discuss the following with firms:

- a) Operational and legal build plans including timeline to meet Art 39 for each relevant CCP
- b) Client outreach programme
- c) Firms' engagement with the CCPs and their plans to address information gaps where they still exist

CMs not incorporated in the UK were invited to contact their own regulators to discuss the same issues with them – so inwardly passported firms need not contact the FCA.

4. Excess management

The FCA said that further guidance will be forthcoming in the next round of ESMA Q&As* around the definition of excess/what constitutes excess. This will build on what is already defined in the Q&As.

In terms of the actual management of excess, FCA said that firms should ensure that any

arrangements around the management of excess should be agreed with clients and stipulated in contractual terms of business documentation – so for example, if funds were received from a client post CCP cut-off, then these funds should be held in accordance with protection agreed in the client's ToB – TTCA/CASS – pending posting to a CCP.

5. Client allocations management

During the last meeting with the NCAs, the FOA raised the question of how unallocated client trades should be 'held' pending give-up allocations or pending acceptance by a clearing member. The FCA said that a trade executed on behalf of a client should be viewed as a 'client' trade even though that trade may not have been booked to the actual client account. As a result, such trades should be booked to a 'Client Account' at the CCP but not the Client Omnibus Account – i.e the CCP would need to offer a separate omnibus account for unallocated trades funded by the clearing member.

In response to the related question around what should firms do if the CCP doesn't offer more than one omnibus account, FCA responded by saying that CCPs must offer multiple omnibus accounts in order to get re-authorised under EMIR.

6. US/EU regulatory conflicts

In response to the concerns FOA had raised earlier regarding conflicts between US bankruptcy law and US FCMs having to comply with EMIR segregation obligations, the FCA stated that this would be covered by a Q&A in the next ESMA Q&As*. The FCA was asked for a steer on how this would be addressed in the Q&As. The FCA responded that they could not provide any further information but they did say that, although the Q&A would NOT change their interpretation of Article 39 and the scope of its application, they thought that the industry would find it helpful in addressing the regulatory conflicts we had raised.

7. CCP re-authorisation process

The FCA were asked whether they could comment on the recent announcement by Nasdaq OMX that their application for re-authorisation would be subject to an additional delay following a further information request by the College after their application had been deemed complete. The FCA and the BoE said that any queries should be addressed to NOMX.

8. AOB

EMIR Art. 39(7) Disclosures: The FCA welcomed the work that was being done to draft a standard industry disclosure document but urged the FOA/ISDA to engage with the buy-side to ensure that it met their expectations. The FCA stated that they would like to have a separate meeting with FOA to discuss this further.

* New ESMA Q&As – the next set of draft ESMA Q&As go before the Board of Supervisors on 7 November 2013 and therefore it is expected that the new Q&As will be published by 15 November 2013.