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17 November 2021

Dear Commissioner McGuinness,

Dear Chairman Campa,

Dear Chairwoman Hielkema,

Dear Chairwoman Ross,

EMIR – Time-limited derogation under the Margin and Clearing Regulatory Standards (Margin RTS and Clearing RTS) for intragroup transactions

The Joint Associations¹ welcome the steps that the European Commission and European Supervisory Authorities (ESAs) have taken so far to ensure that EU entities can rely on the intragroup exemption from clearing and margin requirements under EMIR when entering into OTC derivatives with non-EU affiliates, introducing a temporary derogation from the requirement to have an equivalence decision in place under Article 13 EMIR in respect of the relevant non-EU jurisdiction. We particularly welcome the publication of the revised Margin RTS and Clearing RTS on 17 February, extending the temporary intragroup derogation until 30 June 2022.

We also support the adoption of equivalence decisions for the US Prudential Regulators, Australia, Brazil, Canada, Hong Kong and Singapore with respect to margin requirements, although as discussed further below – and in previous correspondence - we have some concerns regarding the detail of these equivalence decisions.

However, the Joint Associations would like to take this opportunity to emphasise the continued importance of intragroup transactions both for the ability of EU financial and non-financial groups to operate, compete (with other comparable groups) and make capital available in non-EU jurisdictions and to manage risks on a centralised basis. Intragroup transactions are also vital to enable non-EU financial and non-financial groups to provide capital needed to underpin investment within the EU-27, and to manage risk associated with this activity.

As the current intragroup derogation in relation to the clearing and margin obligations is set to expire in June 2022, we ask that:

- 1) The Commission adopt equivalence decisions as a matter of urgency in relation to all jurisdictions that have implemented clearing obligations and/or margin obligations in line with the G20 commitments;

¹ The Joint Associations are EACB, EBF, EFET, FIA, GFMA, ISDA and NSA. Information on each association is set out in the Annex to this letter.

- 2) The Commission address the practical difficulties and level playing field issues associated with EMIR Article 13 equivalence; and
- 3) The Commission and ESAs amend the Clearing and Margin RTS to extend the current intragroup derogation from clearing and margin requirements for a further 3 years for all jurisdictions where an equivalence decision is not available, thereby avoiding a cliff edge after 30 June 2022, when EU firms and international firms providing liquidity in the EU27 would face a significant financial and risk management impact as well as other burdensome compliance requirements as a result of expiry of the derogations (as outlined in more detail in the following sections of this letter).

1. Executive summary

Extension of the intragroup derogation: We would ask the European Commission and ESAs to extend the temporary intragroup derogations for the clearing and margin obligations beyond June 2022 for a further 3 years, in order to give certainty to EU firms and to ensure a level playing field between EU firms whose group is entirely within the EU and EU firms that operate on a global level.

Importance of intragroup transactions to EU entities: Intragroup transactions are an essential part of centralised risk management by EU entities which operate on a cross-border basis, which in turn allows EU firms and financial markets to remain competitive. Intragroup transactions are also a key part of implementing mandatory clearing requirements, as not every firm in a group can become a clearing member of the relevant CCPs. If the temporary derogations are allowed to expire without being replaced by equivalence decisions in all key jurisdictions, this will result in increased costs and operational burdens for EU firms while also resulting in trapped assets.

Practical difficulties with application of equivalence regime under Article 13 EMIR: We would also welcome clarification on how to deal with a number of practical difficulties and level playing field issues that arise with respect to the equivalence regime under Article 13 EMIR, which have an impact on the ability of EU firms to rely on the intragroup exemptions in the absence of the temporary derogation.

2. Extension of the current intragroup derogations

The Clearing and Margin RTS currently provide for temporary intragroup derogations from the clearing and margin obligations, so that where an EU counterparty and a third-country counterparty to an OTC derivative subject to the clearing obligation or margin requirements meet the conditions for an intragroup transaction, and where no equivalence decision has been adopted in respect of the relevant third country under Article 13(2) of EMIR, the clearing obligation and margin requirements shall take effect from a date 3 years after the date of entry into force of the relevant Clearing RTS. These temporary intragroup derogations are currently set to expire on 30 June 2022.

We are concerned that it will be necessary to extend the temporary derogations further in order to protect EU counterparties which enter into OTC derivatives with non-EU affiliates located in jurisdictions which have adopted clearing and margin requirements but for which the European Commission has not adopted an equivalence decision by 30 June 2022² and in jurisdictions which have not yet adopted clearing and margin requirements equivalent to those under EMIR. Even if equivalence decisions will be adopted for a number of other G20 jurisdictions, the justification for having a derogation for cross-border intragroup transactions will continue to exist for many other jurisdictions. If the derogations are not extended, the impact on the ability of European derivative market participants to operate on a cross-border basis would be severe, and would come at a time when the European economy is still recovering from the impact of the COVID pandemic.

In order to address the risk of market fragmentation and instability resulting from termination of the temporary derogations in the absence of sufficient and scalable equivalence decisions, we would ask the European Commission and ESAs to take steps urgently to extend the temporary derogations beyond 30 June 2022, in order to ensure that EU firms have certainty regarding their continued ability to rely on these derogations and in order to ensure a level playing field between EU firms whose group is entirely within the EU and EU firms which operate on a global level and so have affiliates in multiple non-EU jurisdictions.

We would ask the European Commission and ESAs to consider extending the temporary derogations for a further 3 years.

A 3 year extension would ensure that the temporary derogations remain in place until the Commission has had the opportunity to conduct its next scheduled review of the Level 1 text of EMIR (which is to be completed by 18 June 2024). This would enable the Commission to make any appropriate amendments to EMIR at that point to address the difficulties arising from the current operation of the intragroup exemptions.

Such an extension would also allow time for the European Commission to continue its work on assessment of the appropriateness of finding these jurisdictions equivalent, mitigating the challenges associated with equivalence under EMIR Article 13. It would also allow other important jurisdictions more time to develop their regulatory frameworks with respect to OTC derivatives business, such that they are more aligned with the EU standards. Such an extension of the derogations would also maintain the competitiveness of EU supervised entities engaged in derivatives business with and in these third countries.

If the EU applies the clearing obligation and margin requirements to cross-border intragroup transactions it will be an outlier in comparison with other major jurisdictions

The clearing obligations of other key jurisdictions (including other G20 jurisdictions) provide exemptions for transactions between affiliates. In this regard, we would ask the European

² For example, the SEC margins rules, published in 2019 and in force since 1 November 2021, are not subject to an equivalence decision under article 13 of EMIR

Commission to consider – for the purpose of future revision of EMIR Level 1 - whether it continues to be appropriate for EMIR to require OTC derivatives transactions between affiliates to be cleared through a CCP or whether it would be appropriate to amend EMIR Level 1 to provide a permanent exemption for transactions which qualify as intragroup transactions.

With respect the exchange of IM and Variation Margin (VM) in relation to transactions between affiliates, the EU would be an outlier, creating an unlevel playing field to the detriment of EU firms. The margin rules of the US CFTC and SEC, Brazil, Canada, Hong Kong, Japan, Singapore and South Korea do not require any exchange of margin between affiliates. It is important to note that the US prudential regulators, following a finale rule³ published on 1st July 2020, only require the exchange of IM and VM in limited circumstances. Similar limitations can be observed for the Australian margin rules.

3. Importance of intragroup transactions to EU entities which operate on a cross-border basis

Intragroup transactions are crucial for centralised risk management at group level by EU entities which operate on a cross-border basis

Intragroup transactions are an essential tool for enabling financial and non-financial groups to offer derivatives business across borders⁴. They allow central management of risk and liquidity, which is key to enabling investment firms to offer the most favourable prices to their clients. The ability of EU firms to carry out intragroup transactions without being required to clear or margin those transactions allows EU financial markets to remain competitive. If this was not the case, the collateral cost to EU firms would make central risk management models prohibitively costly and impede their ability to operate and compete in international derivative markets. We discuss the reasons for this cost increase further below.

International financial and non-financial groups operate through a network of subsidiaries and branches, both within the EU and across third countries. This network allows international groups to operate in different markets, with the various entities and branches facing clients, and counterparties in multiple localities. However, in order to offer liquidity in multiple jurisdictions, international financial and non-financial groups need to be able to centrally manage the risk associated with cross border trading.

It is common for risk to be centrally managed in both financial and non-financial groups. This allows for more efficient hedging and management of the risks that the group is exposed to. It also enables the use of central infrastructure, rather than having to build separate systems in

³ <https://www.federalregister.gov/documents/2020/07/01/2020-14097/margin-and-capital-requirements-for-covered-swap-entities>

⁴ See further discussion in the Joint Associations' letters of 30 April 2020 (with respect to the Margin RTS <https://www.isda.org/a/GDQTE/Joint-Association-Letter-on-Margin-Intragroup-Exemption.pdf>) and 2 June 2020 (with respect to the Clearing RTS <https://www.isda.org/a/pibTE/ISDA-FIA-EBF-Letter-on-Derogation-of-EMIR-Clearing-Obligation-for-Intragroup-Transactions.pdf>)

each jurisdiction in which group entities operate, without compromising on risk management or on compliance with regulatory obligations in the jurisdiction they are trading in. Rather, booking models are used which allow effective management of prudential risks to the group, and central management of derivative risk.

The management of this risk is facilitated by trades between group entities. These are not client facing trades, are not price forming, and do not alter the market or credit risk exposure. Rather, they are a transfer of risk within the group. Client/counterparty facing trades would remain subject to clearing or margin requirements, where those trades fall in scope of the relevant requirement.

Intragroup transactions are key to implementing the clearing obligation

Intragroup transactions are also important for firms to implement mandatory clearing requirements. Local market regulation often requires market participants to interact with locally established firms (as opposed to international firms without a place of business in that jurisdiction), which may be subsidiaries of international groups but which may not themselves be clearing members (or may not be able to become clearing members). If the trades involved fall into a class of derivatives subject to the clearing obligation, the local firm will have to clear the transaction via a subsidiary within the group (or even a third party) which is a clearing member.

The costs incurred in relation to each cleared transaction include clearing fees, capital cost, increase in default fund contribution, initial margin requirements and related funding costs. These costs are likely to be increased during periods of market stress, as seen during the COVID-19 related market turmoil where large price movements prompted large margin calls from central counterparties (CCPs).

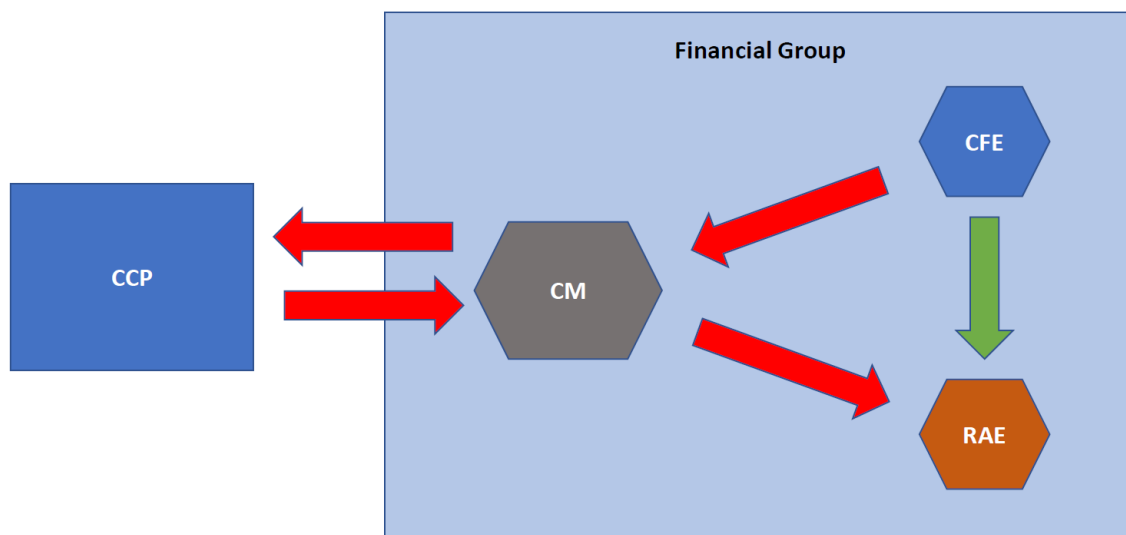
If the current intragroup derogation is not renewed, this could also create obstacles to facilitating client clearing for non-intragroup transactions as well, as a result of the substantial increase in collateral that will need to be assigned to clearing, as well as other constraints such as leverage ratio and balance sheet size. All of this will reduce clearing capacity in the system.

4. Allowing the current intragroup derogations to expire may increase costs for EU entities and give rise to risks specific to intragroup transactions

Requiring clearing of intragroup transactions would create more operational risk and have little benefit in terms of reducing counterparty risk

There is a strong argument that requiring clearing of intragroup transactions will actually increase risk (undermining the aims of EMIR). A clearing requirement would have to be applied unnecessarily to these transactions, creating the necessity for multiple additional transactions with the CCP, with the extra operational and counterparty risk this implies.

Most groups will have only a small number of entities that are direct or indirect clearing members of a CCP. In some group structures, these CCP clearing members are not the group's risk aggregation entities, nor are they client/counterparty-facing entities. Thus, in the absence of an exemption, an intragroup transaction between a client/counterparty facing entity ('CFE') and a risk aggregation entity ('RAE') would have to be cleared by both CFE and RAE. To do this, each of these entities would have to transact with the group's clearing member ('CM'). This means that one trade, between the CFE and the RAE, would effectively generate four separate transactions, CFE to CM, CM to CCP, CCP to CM, and CM to RAE. Depending on how the CM has organised the client clearing accounts for group companies, these two transactions (CFE-CM and RAE-CM) are likely to net out in an omnibus account at the group CM. The clearing requirement therefore would likely add no benefits in terms of risk reduction, but would add additional operational effort and risk.



In addition, if a contract falls within the scope of the clearing obligation it will be cleared at least once. Typically, if it is (1) a dealer-to-dealer contract, clearing will result in each dealer facing the CCP where each dealer is a CM at the CCP in question. If it is (2) a client trade – with the client subject to a clearing requirement – then the client will face the group CM who will present the trade to the CCP for clearing and the appropriate segregation model will apply for this trade. For both types of trade - either (1) dealer-to-dealer or (2) dealer-client - one of the entities within the group is clearing the trade facing the CCP. If that entity then reallocates that risk to another entity within the group it should not be required to clear that trade yet again.

Requiring exchange of margin for intragroup transactions would give rise to trapped assets and significant increased costs for EU entities

If the current margin intragroup derogation is allowed to expire, the expectation is that EU firms will have to exchange Initial Margin (IM) when trading with their non-EU affiliates and that the amount of margin that will need to be exchanged will be a further 25 – 35% of the

margin already being exchanged with external clients. This margin would be posted in segregated, bankruptcy-remote form not capable of being rehypothecated (meaning that the margin is trapped liquidity or assets which cannot be used for any other purpose). This will increase the funding costs of each firm, as well as imposing an opportunity cost (as the assets cannot be put to more productive use, such as financing real economy activities). There will also be an operational and staff cost, as additional systems and human resource will need to be deployed at affiliates to manage and oversee the margin exchange process and to monitor reporting of margin exchanged. Aside from the increased cost, this will also have an impact on the competitiveness of EU firms in global markets, as the increase in costs will ultimately impact the price at which EU firms can offer services to clients.

The potential compliance requirements associated with the loss of the intragroup derogations are legally, operationally and financially demanding and will take many months to put in place.

Withdrawal of the intragroup derogation from the clearing obligation would also trigger the trading obligation under Art 28 MiFIR

The technical standards specifying the classes of derivatives subject to the trading obligation state that the trading obligation shall take effect from the later of 3 January 2018 or "the date referred to in Article 3 of [the relevant clearing RTS] for that category of counterparties".

Article 3 of each of the Clearing RTS is the provision that creates the current intragroup derogation, meaning that so long as the intragroup derogation is available in relation to the clearing obligation, it will also be available in relation to the trading obligation.

As a result, the removal of the intragroup derogation for transactions involving a third-country entity would bring those transactions into the scope of the trading obligation as well as the clearing obligation. This would be contrary to the protections built into MiFIR, as it would potentially require large non-price forming trades to be executed on-venue. In addition, requiring intragroup transactions to take place on a trading venue is likely to further exacerbate the issues outlined above regarding increased costs and the impact on competitiveness of EU firms in global markets.

5. Application and availability of equivalence under Article 13 EMIR

Concerns with the application of the equivalence regime under Article 13 EMIR

As outlined in ISDA's letter to Commissioner Mairead McGuinness of 27 September 2021, there are a number of practical difficulties and level playing field issues with respect to the equivalence regime under Article 13 EMIR equivalence, including:

- The potential effect of the word "established" in Article 13 EMIR and any equivalence decisions made under Article 13;

- The requirement for "at least one counterparty" to be both established in the US and considered a Covered Swap Entity in the Article 13 equivalence decision for the US Prudential Regulators (and similar requirements in other equivalence decisions);
- The application of intragroup exemptions under EMIR and CRR that are dependent on Article 13 equivalence.

Each of these points is discussed further in the letter mentioned above.

Availability of equivalence decisions for all relevant jurisdictions

The original purpose of the temporary derogation included in the Clearing and Margin RTS was to give the European Commission time to adopt equivalence decisions in relation to any relevant third countries. However, while ESMA has delivered technical advice regarding the equivalence of the clearing obligations in a number of jurisdictions, no equivalence decisions have yet been adopted. While many jurisdictions only completed implementation of their own clearing rules after adoption of the Clearing RTS, a significant number of jurisdictions have now had clearing obligations in force for several years, including Argentina, Australia, Canada, Hong Kong, India, Japan, Mexico, PRC, Singapore, South Africa, South Korea, Switzerland and the United Kingdom. These jurisdictions are important trading partners of the EU and important markets for EU financial institutions and non-financial entities.

For some very small or closed jurisdictions (e.g. jurisdictions employing currency or capital controls), it may not be appropriate or efficient to apply a clearing obligation locally (see the ISDA paper "Clearing in Smaller or Closed Jurisdictions"⁵). Such jurisdictions may not ever adopt a clearing obligation. As such, we believe consideration should be given as to whether it is appropriate at all to expect intragroup transactions involving group entities located in such jurisdictions to be cleared.

We thank you for taking the time to consider our views on this issue. If you have questions on any of the issues addressed in this letter, we are happy to discuss them with you at your convenience.

Yours sincerely,

⁵ <https://www.isda.org/a/tsvEE/ITC-Small-Jurisdictions-final.pdf>

Nina Schindler

CEO

EACB



Wim Mijs

CEO

EBF



Mark Copley

CEO

EFET



Walt Lukken

President and CEO

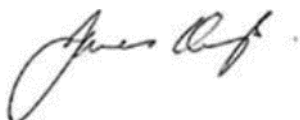
FIA



James Kemp

Managing Director

Global Foreign Exchange Division, GFMA



Scott O'Malia

CEO

ISDA

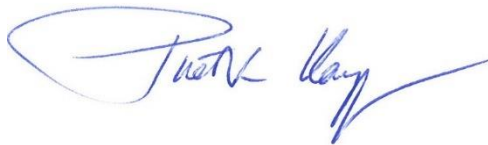
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Piia-Noora Kauppi

Managing Director

Finance Finland

(current Presidency of NSA)

A handwritten signature in blue ink, appearing to read "Piia-Noora Kauppi".

Annex

About EACB

The European Association of Co-operative Banks ([EACB](http://www.eacb.coop)) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 28 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4,050 locally operating banks and 58,000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 210 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 79 million members and 749,000 employees and have a total average market share of about 20%. Website: www.eacb.coop

About EBF

The European Banking Federation is the voice of the European banking sector, bringing together 32 national banking associations in Europe that together represent a significant majority of all banking assets in Europe, with 3,500 banks - large and small, wholesale and retail, local and international – while employing approximately two million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that reliably handle more than 400 million payment transactions per day. Launched in 1960, the EBF is committed to a single market for financial services in the European Union and to supporting policies that foster economic growth.

About EFET

The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or other undue obstacles. We build trust in power and gas markets across Europe, so that they may underpin a sustainable and secure energy supply and enable the transition to a carbon neutral economy. EFET currently represents more than 100 energy trading companies, active in over 27 European countries. For more information: www.efet.org

About FIA

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and

commodities specialists from more than 48 countries as well as technology vendors, lawyers and other professionals serving the industry.

FIA's mission is to:

- support open, transparent and competitive markets,
- protect and enhance the integrity of the financial system, and
- promote high standards of professional conduct.

As the leading global trade association for the futures, options and centrally cleared derivatives markets, FIA represents all sectors of the industry, including clearing firms, exchanges, clearing houses, trading firms and commodities specialists from more than 48 countries, as well as technology vendors, lawyers and other professionals serving the industry.

About the GFXD

The Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) was formed in co-operation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 23 global foreign exchange (FX) market participants, collectively representing the majority of the FX inter-dealer market⁶. Both the GFXD and its members are committed to ensuring a robust, open and fair marketplace and welcome the opportunity for continued dialogue with global regulators.

About ISDA

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 960 member institutions from 77 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter @ISDA.

About NSA

The Nordic Securities Association (NSA) is a Nordic cooperation that works to promote a sound securities market primarily in the Nordic region. The NSA is formed by the Danish Securities Dealers Association (Børsmæglerforeningen), Finance Finland (Finanssiala), the Norwegian Securities Dealers Association (Verdipapirforetakenes Forbund) and the Swedish Securities Dealers Association (Svenska Fondhandlareföreningen). Website: www.nsa-securities.com/

⁶ According to Euromoney survey