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COMMISSION DELEGATED REGULATION (EU) .../...

of 24.9.2021

supplementing Regulation (EU) 2019/2033 of the European Parliament and of the Council with regard to regulatory technical standards specifying the amount of total margin for the calculation of the K-factor “clear margin given” (K-CMG)

(Text with EEA relevance)

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE DELEGATED ACT

Article 23(3) of Regulation (EU) 2019/2033 ('the Regulation') empower the Commission to adopt, following submission of draft standards by the European Banking Authority (EBA), and in accordance with Articles 10 to 14 of Regulation No (EU) 1093/2010, delegated acts to specify the calculation of the amount of the total margin for the calculation of K-CMG.

In accordance with Article 10(1) of Regulation No (EU) 1093/2010 establishing the EBA, the Commission shall decide within three months of receipt of the draft standards whether to endorse the drafts submitted. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT

In accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has carried out a public consultation on the draft technical standards submitted to the Commission in accordance with Article 23(3) of the Regulation. A consultation paper was published on the EBA internet site on 4 June 2020, and the consultation closed on 4 September 2020. Moreover, the EBA worked in consultation with European Securities and Markets Authority (ESMA), invited the EBA's Banking Stakeholder Group set up in accordance with Article 37 of Regulation No (EU) 1093/2010 to provide advice on them. Together with the draft technical standards, the EBA has submitted an explanation on how the outcome of these consultations has been taken into account in the development of the final draft technical standards submitted to the Commission.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation No (EU) 1093/2010, the EBA has submitted its Impact Assessment, including its analysis of the costs and benefits, related to the draft technical standards submitted to the Commission. This analysis is available at <https://eba.europa.eu/regulation-and-policy/investment-firms/regulatory-technical-standards-prudential-requirements-investment-firms>, pages 60-85 of the Final Draft Regulatory Technical Standards package.

3. LEGAL ELEMENTS OF THE DELEGATED ACT

The Delegated Act specify the calculation of the amount of the total margin required for the calculation of K-factor 'clearing margin given' (K-CMG) on a portfolio basis, and the conditions for the fulfilment of the provisions regarding regulatory arbitrage avoidance.

For the purpose of the calculation the amount of the total margin required by the clearing member from the investment firm, the Delegated Act specify that the amount of total margin shall be the required amount of collateral (comprising initial margin, variation margins and other financial or non-financial collateral), in accordance with the clearing member's margin model.

When an investment firm uses multiple clearing members, the Delegated Act prescribe that the K-CMG is measured by calculating on a daily basis the sum of the total margins required by each clearing member over the preceding three months, then determining the third highest amount, and then multiplying the outcome by the 1.3 coefficient prescribed in the Regulation.

Furthermore, the Delegated Act specify a set of criteria that the competent authority has to assess when determining if the choice of the portfolios for which the K-CMG is used has been made with a view to engaging in regulatory arbitrage.

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014¹, and in particular the third subparagraph of Article 23(3) thereof,

Whereas:

- (1) For the purposes of specifying the calculation of the amount of the ‘total margin required’, referred to in Article 23(2) of Regulation (EU) 2019/2033, and in order to increase clarity and consistency in relation to its components, it should be clarified that the amount of the total margin required includes any collateral required by the clearing member in accordance with its margin model.
- (2) In accordance with Article 23(2) of Regulation (EU) 2019/2033, the total margin required on a daily basis is used for the calculation of K-CMG. Where clearing members adapt their required margin within one day, this results in more than one margin call within the same day. In order to avoid uncertainty about which of those margin requirements to use and considering that the third highest amount during a period of three months is to be used for the calculation of K-CMG, it is necessary to specify that the daily amount of margin required should be the highest of those margin requirements of a given day.
- (3) Investment firms may use the clearing services of multiple clearing members. For positions for which K-CMG is applied, the determination of the amount of total margin required from the investment firm should be comprehensive and include the full margin required by all clearing members. Therefore, where an investment firm uses K-CMG for positions that are subject to clearing by multiple clearing members, CMG should be calculated as the sum of the margins required across all clearing members. An investment firm should, accordingly, first calculate the total daily amount of margin required as the sum of the total margin required by all clearing members, before determining the third highest amount of total margins required on a daily basis as required by Article 23(2) of Regulation (EU) 2019/2033.
- (4) For the application of K-CMG on a portfolio basis, where the whole portfolio is subject to clearing or margining, the conditions laid down in Article 23(1) of Regulation (EU) 2019/2033 have to be met. Therefore, a portfolio of cleared positions

¹ OJ L 314, 5.12.2019, p. 1.

assigned to one trading desk can make use of K-CMG while, at the same time, a portfolio of cleared positions assigned to another trading desk can make use of the K-factor 'net position risk' (K-NPR). In order to prevent arbitrage, the use of K-CMG and K-NPR across trading desks should be consistent. Therefore, the same approach should be used for trading desks that are similar in terms of business strategy and trading book positions.

- (5) For the purposes of the assessment under Article 23(1), point (e), of Regulation (EU) 2019/2033, the competent authority should be required to assess whether the K-CMG approach is appropriate insofar it reflects the risk profile of the investment firm's trading book positions. An investment firm should be required to compare regularly its own risk assessment with the margins required by clearing members, for the purpose of assessing whether those margins are still a good indicator of the level of risk to market of the investment firm. At the point of assessment by the competent authority, the investment firm should make a comparison between the capital requirements under K-NPR and K-CMG and should be able to adequately justify the difference between those capital requirements to the competent authority. An assessment by the competent authority should be positive only when all these conditions are met. In particular, the competent authority should ensure that the investment firm is able to monitor and adequately justify difference between the outcome of the two methodologies, K-NPR and K-CMG, especially in cases of large variations of the required margins.
- (6) A high frequency of switching between the use of K-NPR and K-CMG is a strong indicator of potential disproportionate or unsound use of own funds requirements. It is possible to prevent regulatory arbitrage by constraining the frequency of switching positions between the use of K-NPR and K-CMG. A requirement to make continuous use of one of the two methods for a trading desk for at least two years would be proportionate to address the risk of regulatory arbitrage. However, in exceptional cases (e.g. a business restructuring) where a trading desk changes to such an extent that it can be considered as a different trading desk, the competent authority should allow an investment firm to change methods within that two-year period.
- (7) This Regulation is based on the draft regulatory technical standards submitted to the Commission by the European Banking Authority (EBA).
- (8) The EBA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the advice of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council²,

HAS ADOPTED THIS REGULATION:

Article 1

Calculation of the amount of the total margin required

1. The amount of the total margin referred to in Article 23(2) of Regulation (EU) 2019/2033 shall be the required amount of collateral comprising the initial margin, variation margins and other collateral, as required by the clearing member based on its margin model of the investment firm for the trading desks subject to K-CMG. For

² Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

the purposes of this Regulation, ‘trading desk’ shall mean a trading desk as defined in point (144) of Article 4(1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council³.

2. Where the clearing member does not differentiate between margins that are required for the trading desk that is subject to K-CMG and margins that are required for other trading desks, the investment firm shall consider the total of margins required for all trading desks as margins under paragraph 1.
3. Fees paid by the investment firm to the clearing member for making use of its clearing member services shall not be considered as margins under paragraph 1.
4. Where the clearing member updates the total margin required more than once during a day, the total margin required on that day shall be the highest of those amounts of total margins required by the clearing member during that day.
5. Where an investment firm makes use of the services of more than one clearing member for the trading desks subject to K-CMG, the amount of the total margin referred to in Article 23(2) of Regulation (EU) 2019/2033 shall be calculated on a daily basis adding the amounts of margins required by each clearing member as laid down in paragraph 1 of this Article.

Article 2

Prevention of arbitrage

1. The requirement laid down in Article 23(1), point (e), of Regulation (EU) 2019/2033 shall be fulfilled where all the following conditions are satisfied:
 - (a) where the investment firm calculates K-CMG capital requirements on a portfolio of cleared positions assigned to one trading desk, it applies the same methodology to all the positions of that trading desk for a continuous period of at least 24 months or the business strategy or operations of the group of dealers of that trading desk has changed to the extent that they can be considered a different trading desk;
 - (b) the investment firm uses K-CMG consistently across trading desks that are similar in terms of business strategy and trading book positions;
 - (c) the investment firm has policies and procedures in place showing that the choice of portfolio(s) subject to K-CMG would reflect the risks of an investment firm’s trading book positions, including the expected holding periods, the trading strategies applied and the time it could take to hedge out or manage risks of its trading book positions;
 - (d) the investment firm has policies and procedures in place enabling it to compare the capital requirements calculated on the basis of K-CMG with the capital requirements calculated on the basis of K-NPR and to adequately reasoning any difference between them taking into account the factors set out in paragraph 2 in each of the following cases:

³ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

- (i) where a change in the business strategy of a trading desk results in a change of 20 % or more in the capital requirements for that trading desk based on the K-CMG approach;
 - (ii) where a change in the clearing member's margin model results in a change in the margins required of 10% or more for the same portfolio of underlying positions for a trading desk;
 - (e) the investment firm makes use of the outcome of the K-CMG calculation in its risk management framework and regularly compares the results of its own risk assessment with the margins required by clearing members;
 - (f) the investment firm has compared the capital requirements calculated by K-CMG with the capital requirements calculated by K-NPR for each trading desk at the point of the assessment by the competent authority, and has provided the competent authority with adequate justification of any difference between them taking into account the factors set out in paragraph 2.
2. For the purposes of paragraph 1, points (d) and (f), the competent authority shall take into account the following factors in order to assess whether the difference in capital requirements calculated in application of K-CMG and K-NPR is justified:
- (a) the reference to the relevant trading strategies;
 - (b) the investment firm's own risk management framework;
 - (c) the level of the investment firm's overall own funds requirements calculated in accordance with Article 11 of Regulation (EU) 2019/2033;
 - (d) the results of the supervisory review and evaluation process, if available.

Article 3
Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 24.9.2021

For the Commission
The President
Ursula VON DER LEYEN