

Harmonisation of critical OTC derivatives data elements (other than UTI and UPI) – third batch – consultative report

Respondent name:

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General comments on the report

First of all, besides the fact that, in Brazil, every OTC derivative transaction must be registered in Trade Repositories to be considered legally valid, it must be pointed out that in the Brazilian financial market there is no legal obligation to collateralize OTC derivatives (within non CCP environments) and its registration, if it exists, is not necessary as well. However, initiatives as this Consultative Report is relevant in order to create a global standard of capturing and storing derivatives data elements and its collaterals, mainly with the objective to provide more governance to each jurisdiction regulators.

2.1 Collateral portfolio

Comments on the data element "collateral portfolio":

Currently, B3 offers to its customers a solution to register collateral involved in derivatives transactions. Besides that, the solution has no link among the collateral informed and the correspondents contracts guaranteed by them. That is the reason why collateral management system is not aware of the OTC derivatives transactions created under the same Master Agreement as the concept of "collateral portfolio code" is not applied. It would be reasonable having the information if the collateral informed is part of a portfolio or not. It would bring a more accurate analysis related to the constitution of the guarantee.

2.2 Collateral portfolio code

Q1: With reference to the alternatives proposed to capture information on portfolio code(s) (Section 2.2):

- (a) In your view, how prevalent is the situation in which different transactions concluded under the same Master Agreement are associated with different CSAs (for initial margin posted, initial margin received and variation margin)?

As B3's collateral management system does not have details related to Master Agreements (MA) and the possible OTC derivatives transactions created under that MA, the concept of "collateral portfolio code" is not applied. Because of that, capturing the associations among different CSAs for a specific MA is very complex.

- (b) The definition proposed in Alternative 1 is based on the assumption that, in the event of default, the entirety of the collateral provided under the given Master Agreement would be used to cover the loss of the non-defaulting counterparty, whether or not separate CSAs (for initial margin posted, initial margin received and variation margin) might be linked to that Master Agreement and whether or not all the transactions concluded under that Master Agreement would be associated with each of these CSAs. Is this assumption correct? If not, please clarify how the respective obligations would be resolved in the case of default. Please provide examples.

Yes, we understand that this assumption is correct.

(c) Are the differences in authorities' use of the two alternatives clearly illustrated in Table 2?

Yes, the alternatives are clearly illustrated in Table 2.

(d) Which of the proposed harmonisation alternatives should be supported and why?

We believe that alternative 1 would be the most appropriate suggestion in that case. The alternative 2 wouldn't be applicable to the Brazilian market as the transactions are not segregated by margin type. The margin type (initial or variation margin) is constituted by bilateral relation on the OTC market, and as mentioned before the complexity to capture the segregated data related to association of Master Agreement and CSA could make the alternative 2 unfeasible.

Other comments on the data element "Collateral portfolio code":

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2.3 Portfolio containing non-reportable component

Comments on the data element "Portfolio containing non-reportable component":

The data element is pertinent, however, as it is hard to control the transactions related to a specific collateral portfolio, probably having that in the short time could not be feasible.

2.4–2.28 Data elements related to margins

Q2: The purpose of the data element "Initial margin settlement timing" (Section 2.10) is to allow authorities to better understand the difference between "Initial margin required to be posted by the reporting counterparty" (Section 2.17) and the "Initial margin posted by the reporting counterparty" (Section 2.5) as this difference may be due to the timing of when the required margin is determined and when the margin is posted. In the absence of information on the margin settlement timing, the difference in the margin required and margin posted amounts could be interpreted as over- or under-collateralisation. Information on the settlement timing of margin collected would serve the same purpose for global aggregation of initial margin collected (Sections 2.8 and 2.19).

- (a) Are there challenges linked to the data element "Initial margin settlement timing" as defined above? Is there an alternative, more effective, way to represent this information, such as the date on which the initial margin posted (or collected) has been settled?

In Brazil, the challenge relies on the fact there is no obligation in the OTC market (non-CCP) that the settlement must happen in a established period of time, even though it's been noticed that the most part of that happens on the same day (T+0). The indicated alternative seems to be the best one in order to obtain such information.

- (b) How prevalent is the existence of different settlement timings (T+0, T+1, T+2, T+3) within a given jurisdiction? Would the settlement timing for the initial margin posted differ from the one for initial margins collected?

Today most settlements regarding margin posted happen on T+0, despite the fact there is no regulatory obligation to do in that timing. The settlement timing for the initial margin posted and the one for initial margin collected could be the same or not, depending on what was agreed by counterparties.

Other comments on the data elements related to margins:

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2.29 Indicator of intraday variation margin calls

Comments on the data element "Indicator of intraday variation margin calls":

There is no intraday margin call for the brazilian OTC market (non-CCP).

2.30 Collateralisation category

Comments on the data element "Collateralisation category":

Currently these classification is not formally used by brazilian institutions, however having such classification seems to be useful in order to have a better understanding of how collateralisation is constituted by market.

2.31–2.35 Data elements related to counterparty rating trigger

Q3: With reference to the data elements "Counterparty rating trigger indicator", "Counterparty rating threshold", "Incremental collateral required", "Threshold rating for automatic termination provision" and "Closeout payment for automatic termination provisions" (Sections 2.31–2.34):

- (a) For each alternative of the data element "Counterparty rating trigger indicator", do definitions and allowable values accurately reflect provisions contained in collateral agreements or master agreements covering OTC derivative transactions to protect parties from counterparty credit deterioration? How prevalent currently are counterparty collateral rating triggers or comparable automatic-termination provisions in collateral agreements or master agreements? How, if at all, have recent changes to market practices affected the

prevalence or the form of counterparty collateral rating triggers or comparable automatic termination provisions?

B3 doesn't have access to the Master Agreement's conditions, as they are established only among counterparties. Currently there is no functionality on B3's systems in order to address this subject or even capture such piece of information. Additionally, there are no requests to such developments.

- (b) Are the advantages and disadvantages of the proposed harmonisation alternatives of the data element "Counterparty rating trigger indicator" appropriately defined? If not, which aspects should be revised and how? Which of the proposed harmonisation alternatives should be supported and why?

Yes, the advantages and disadvantages are appropriately defined. We believe that Alternative 1 is best due to difficulties to adapt in all characteristics and, in our local market lack of rating and specification. Alternative 1 can facilitate comparison and characterization between OTC markets across the globe.

Q4: With reference to the alternatives proposed for the data element "Counterparty rating threshold" (Section 2.32):

- (a) Are the advantages and disadvantages of the proposed harmonisation alternatives appropriately defined? If not, which aspects should be revised and how?

Yes, the alternatives are appropriately defined.

- (b) Which of the proposed harmonisation alternatives should be supported and why?

Alternative 1 seems to be more feasible to be implemented.

Q5: The definition of the data element "Incremental collateral required" (Section 2.33) relies on the assumption that the effects of multiple-notch downgrades are roughly linear. Are there instances in which the effects increase more than linearly with the number of notches in a hypothetical downgrade? If so, how could multiple scenarios be encompassed in the definition?

Currently no credit analysis has been developed on our side. For this reason, the question is being considered as "not applicable".

Other comments on the data elements "Counterparty rating trigger indicator", "Counterparty rating threshold", "Incremental collateral required", "Threshold rating for automatic termination provision" and "Closeout payment for automatic termination provisions" (Sections 2.31–2.35):

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2.36 Clearing obligation in the jurisdiction of the reporting counterparty

Comments on the data element "Clearing obligation in the jurisdiction of the reporting counterparty":

Usually, derivatives transactions once registered in Trade Repositories must be cleared following the rules of such system, and that system also follows jurisdiction rules.

2.37–2.41 Data elements related to “Price”

Q6: With reference to the data element “Price” (Section 2.37), are there OTC derivative transactions products where the price or a concept of price is not captured under the “Price” data element or any other data element including “Fixed rate”, “Spread”, “Strike price”, “Option premium” and “Other payment type (upfront payment)”? If so, please provide detailed examples of those products. Would the industry benefit from additional guidance for the “price” data element?

There is no additional data element related to price that must be part of that list and it is important to consider that having a detailed guidance for the industry would help them to have a better understanding of how to deal with those pieces of information.

Q7: With reference to the data element “Price notation” (Section 2.40), is it clear and unambiguous which price notation (amount or percentage) should be applicable to each price? If not, which ones? Are there additional price notations that should be allowed? If so, which ones? Would the industry rather benefit from additional guidance for the “price notation” data element?

There is no additional data element related to price notation that must be mentioned and it is important to consider that having a detailed guidance for the industry would help them to have a better understanding of how to deal with those pieces of information.

Q8: With reference to the data element "Price unit of measure" (Section 2.41):

- (a) Can commodity derivatives be negotiated in different unit of measures for the price and quantity? If so, would industry support two separate data elements for the (1) Price unit of measure and (2) Quantity unit of measure?

In general commodities are negotiated under the same unit of measures for price and quantity. Unabling the industry to negotiate commodities under different units of measure sounds uncommon.

- (b) The list of allowable values in Table 4 in Annex 1 encompasses all the values included in ISO 20022's Unit Of Measure Code and four additional values.
- (i) Are the values useful for reporting the Quantity Unit of Measure and the Price Unity of Measure?
 - (ii) If not, which ones are less useful and why?
 - (iii) Are there other values that should be added? Which ones, and why?
 - (iv) Are there duplicates or similar values that should be removed?

(iii) Yes, maybe could be added to more units: bags and net arrobas.

In Brazil there's some commodities that are measured in "sacas" (bags, in English), like sugar, coffee, corn and soybean. There's an equivalent measure in metric tons.

And there's another unit of measure called "Arrobas líquidas" (or "net arrobas" in English) used for live cattle contracts. In regarding to this unit, there's also an equivalent in kilograms.

Other comments on the data element "Price", "Price schedules", "Price currency", "Price notation" and "Price unit of measure":

Nothing to add.

2.42–2.50 Data elements related to "Fixed rate", "Strike price" and "Option premium"

Q9: With reference to the data element "Spread notation" (Section 2.45), is it clear and unambiguous which notation (amount or percentage) should be applicable to each spread? If not, which ones? Are there additional spread notations that should be allowed? If so, which ones? Would the industry benefit from additional guidance for the "spread notation" data element?

There is no additional data element related to spread notation that must be allowed, at least by now, and it is important to consider that having a detailed guidance for the industry would help them to have a better understanding of how to deal with those pieces of information.

Other comments on the data element "Fixed rate", "Spread", "Spread currency", "Spread notation", "Strike price", "Strike price currency", "Strike price schedules", "Option premium", "Option premium payment date":

We didn't see any data element regarding to the type of the "spread" or "fixed rate", or the quantity of days in a year. For instance, a 1.20% (per annum) fixed rate could be calculated as a simple or compound rate, and it could be a year of 360 days or 365 days (or even 252 business days in Brazil).

And there's another information that could be introduced to specify the methodology how interest accrues - the counting day fraction. ISDA have some methods, like 30/360 US, 30E/360, 30/360 bond basis, etc.

These two additional information is essential to fully understand the spread or fixed rate and compare or aggregate the data.

2.51–2.52 Data elements related to "Exchange rate"

Comments on the data element "Exchange rate" and "Exchange rate basis":

There are some products (like FX NDF) that doesn't have the exchange rate known in the beginning. The rate will be known in some specific date in the future and it is related to some specific fixing. In these cases, the Exchange Rate is informed as points over or as a percentage of the fixing price in that specific date.

For instance, a FX NDF where the Forward rate will be +0.02 over the FX closing price in T+3.

For that kind of trade, it should be other data elements for "Exchange rate", like "Exchange rate schedule" and "Exchange rate notation".

2.53–2.54 Notional amount and Notional amount schedules

Q10: With reference to the data element "Notional amount" (Section 2.53), are there particular cases where the notional amount may not always be known when a new transaction is reported and may be updated later? If so, which ones?

Nothing to add.

Other comments on the data element "Notional amount" and "Notional amount schedules":

Speaking of notional amount, in Brazil, beside the fact that there is always a notional reported by counterparties, it is possible to have swaps where the notional amount is adjusted during its life cycle depending on the amortization schedule or when the price is known after inception date.

2.55–2.57 Data elements related to “Total notional quantity”

Comments on the data element “Notional quantity schedules”, “Total notional quantity” and “Quantity unit of measure”:

Nothing to add.

2.58–2.63 Data elements related to “Other payments”

Comments on the data elements “Other payment amount”, “Other payment type”, “Other payment currency”, “Other payment date”, “Other payment payer”, “Other payment receiver”:

Nothing to add.

2.64–2.71 Data elements related to “Packages”

Q11: With reference to the data element “Package trade price” (Section 2.66), could it be agreed that two possible situations may arise: (i) a package price does exist because all the transactions that represent individual components of the package are priced jointly, or (ii) a package price is not available because all the transactions that represent individual components of the package are priced individually? Is more clarity needed regarding the reporting of “Package trade price” and prices of individual components?

The package price is provided as described in option (i). As we already have this information as “Package trade price”, we believe that this is the best option.

Other comments on the data elements “Package ID”, “Package trade price”, “Package containing non-reportable components”, “Package trade price currency”, “Package trade price notation”, “Package trade spread”, “Package trade spread currency” and “Package trade spread notation”:

In order to facilitate global aggregation, we recommend the implementation of those data elements.

2.72 Prior UTI

Q12: With reference to the data element “Prior UTI” (Section 2.74), how is “Prior UTI” represented when clearing and allocation happen at the same point in time? And how is “Prior UTI” represented when clearing

and compression happen at the same point in time, as a single event? Do such cases of clearing and compression and clearing and allocation as a single event happen frequently?

Not applicable. Compression functionality is not used in Brazil.

Other comments on the data element "Prior UTI":

Not applicable.

2.73–2.77 Data elements related to "Custom baskets"

Q13: With reference to the data element "Basket constituents unit of measure" (Section 2.74) the list of allowable values in Table 4 in Annex 1 encompasses all the values included in ISO 20022's Unit Of Measure Code and four additional values.

- (a) Are the values useful for reporting the "Basket constituents unit of measure"? If not, which ones are less useful and why?

Yes. ISO 20022 standards are enough.

(b) Are there other values that should be added? Which ones, and why?

No.

Q14: With reference to the data element "Custom basket code" (section 2.75)

(a) would it be preferable to separate the information on the LEI of the basket issuer and the unique alphanumeric code assigned by such issuer to the custom basket? If so, please explain why this would be preferable for global aggregation.

No, It seems that this kind of separation would bring to much complexity for aggregate such information.

- (b) are there types of custom basket for which the "issuer of the custom basket" is not clear? If so, please provide detailed examples of those custom baskets. Would the industry benefit from additional guidance for the term "issuer" in the "Custom basket code" data element?

Not applicable.

- (c) are 52 alphanumeric characters after the LEI of the basket issuer enough?

Yes. LEI is enough.

Other comments on the data elements related to custom baskets:

Not applicable.

Other comments