

EMIR Refit 2.1

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Agenda

- Overview
- Counterparty classification
- Reporting
- Clearing
- Risk mitigation techniques for uncleared trades
(including physically settled FX forwards and swaps)



Overview



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Overview



EMIR Refit published in the Official Journal on 28 May 2019



It will enter into force on 17 June 2019



BUT not all provisions apply on entry into force



Counterparty classification



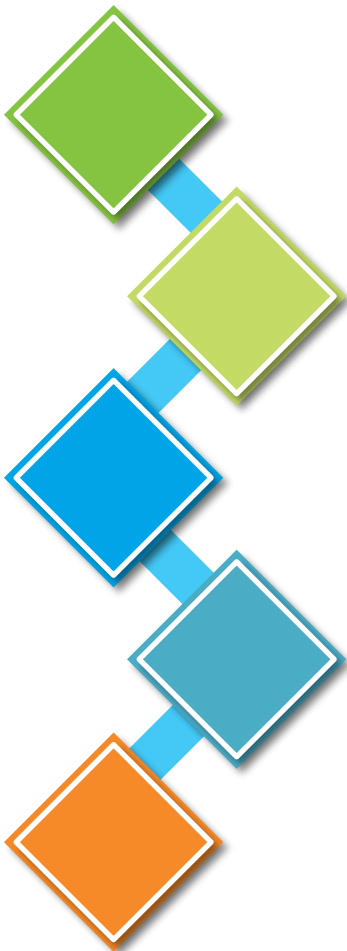
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Current EMIR: What is a non-financial counterparty (NFC) and why do we care?

- Types of NFC: Those who exceed (**NFC+**) and those who fall below (**NFC-**) the “clearing threshold”
- Important as it determines the application of:
 - (a) the clearing obligation; and
 - (b) the level of risk mitigation requirements (including margin)
- Calculation of the “clearing threshold”:
 - Determined by whether the NFC’s rolling average position over 30 working days exceeds the threshold in respect of any one asset class
 - If an entity exceeds the clearing threshold in one asset class, all asset classes in respect of which there is a clearing obligation must be cleared
 - “Clearing thresholds” are: EUR 1 billion for each of credit and equity; EUR 3 billion for each of interest rate, FX and commodity/other
 - Hedging exemption available
 - Group basis: All derivatives contracts entered into by (i) the NFC or (ii) any non financial entities within the group
- Must immediately notify ESMA and the relevant national competent authority (**NCA**) if the clearing threshold is breached



EMIR Refit changes the way the NFC “clearing threshold” is calculated and which transactions must be cleared



Retain concepts of NFC+ and NFC- with certain tweaks

Value of “clearing thresholds”, hedging exemption and group calculation remain unchanged

Changes to calculation of the “clearing threshold”:

- Calculated every 12 months based on the aggregate month-end average position for the previous 12 months
- NFCs are only required to clear an asset class if the clearing threshold is exceeded for that asset class
- NFCs are not required to calculate but if they do not calculate they will be treated as having exceeded the clearing threshold in all asset classes

In addition to notifying ESMA and the relevant NCA if the clearing threshold is breached, must also immediately notify if the calculation is not made

Margin requirements continue to apply to all OTC derivatives if the clearing threshold is breached in one asset class



EMIR Refit introduces the concept of a “clearing threshold” for financial counterparties (FCs)



- New category of small FC (**SFC**) which determines the application of the clearing obligation only
- Margin and valuation requirements apply to all FCs including SFCs
- Same as NFC “clearing threshold” except:
 - Group text includes all entities in the group (not just non-financial entities)
 - No hedging exemption
 - FCs are required to clear all asset classes if the clearing threshold is exceeded in one asset class



The definition of FC has been expanded



- Expanded to include **AIFs established in the EU** in addition to AIFs managed by an AIFM authorised or registered under the AIFMD
- Excludes AIFs and UCITS set up exclusively for the purpose of serving one or more employee share purchase plans
- Does not include securitisation special purpose entities (**SSPEs** - as defined in the AIFMD) including those that are AIFs
- Expanded to include central securities depositories (**CSDs**)
- Key impact for AIFs:
 - **EU AIFs with non-EU AIFMs** will move from NFC to FC
 - **Non-EU AIFs with non-EU AIFMs** will move from TCE NFC to TCE FC



Practical impact of EMIR Refit classification changes



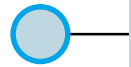
Any status change will be effective from date of entry into force

- ISDA documentation initiatives on classification
- ISDA education letter on AIFs and advocacy for forbearance

Calculation and notification is more prescriptive:

- Calculation of clearing threshold must be made on the date that EMIR Refit enters into force and every 12 months thereafter
- Notification must then be made “immediately” (if the clearing threshold is breached or if the calculation is not made)
- ESMA has published official forms for notifications
- NCAs – e.g. FCA – also publishing forms

Practical impact of EMIR Refit classification changes /continued

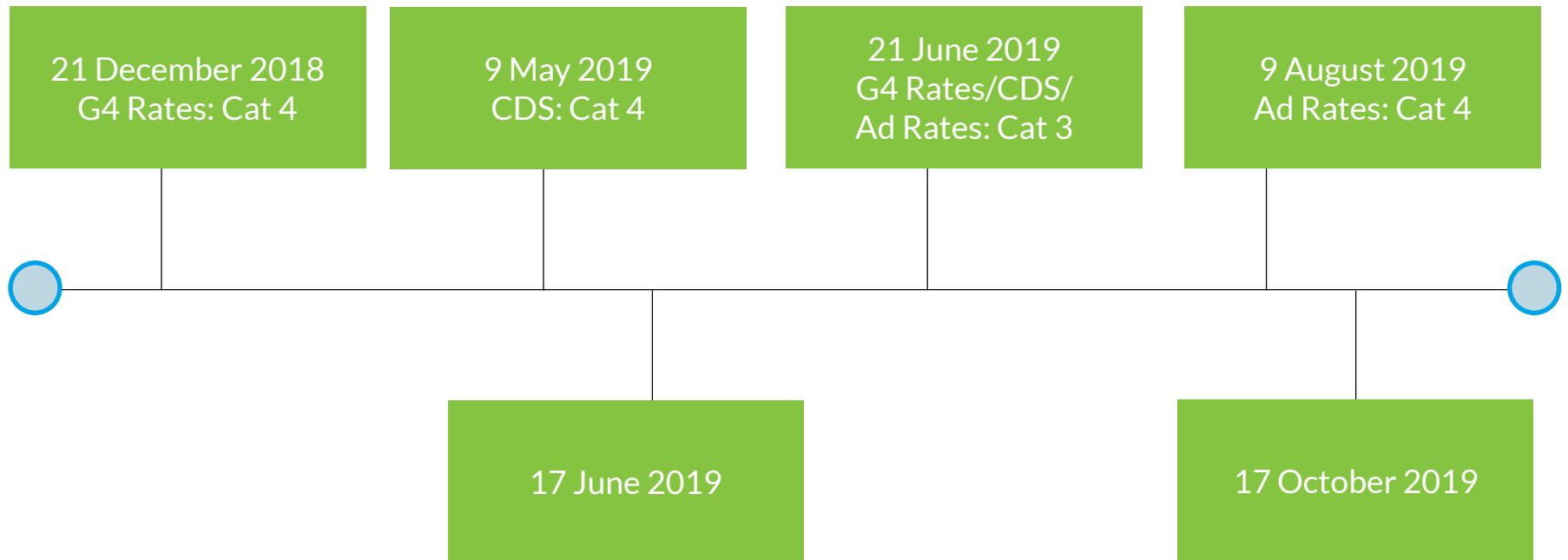


Clearing timing:

- If already subject to clearing, must continue to clear until demonstrate below clearing threshold
- If subject to clearing start date on 21 June, required to start clearing 4 months after the date that EMIR Refit enters into force (17 October)
- Note: Complexity around clearing start dates depending on facts
- ESMA FAQ 28 May 2019
- Impact on trading obligation



Practical impact of EMIR Refit classification changes /continued



Reporting



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Changes to reporting (responsibility and liability for OTC reporting)

FCs responsible and legally liable for OTC reporting for NFC-s and for ensuring data correctness

- NFC-s must provide FCs with information that cannot reasonably be expected to be possessed and ensure its correctness
- NFC- may choose to report on its own behalf (in which case it will be responsible and legally liable and must inform FC in advance)
- NFC-s remain subject to reporting with third country FCs unless third country regime has been deemed equivalent and the third country FC has reported under that regime to a trade repository that is subject to a legally binding and enforceable obligation to grant certain entities direct and immediate access to data

UCITS, AIFs and institutions for occupational retirement provision (IORPs)

- Management company of a UCITS, manager of an AIF and the authorised entity responsible for managing an IORP are responsible and legally liable for OTC reporting on behalf of UCITS, AIFs and IORPs respectively and for ensuring data correctness

Reporting may be delegated

ISDA/FIA Reporting Delegation Agreement likely to be revised

Applies 12 months after entry into force

Within 12 months after entry into force – RTS and ITS on reporting mandated

Within 4 years – ESMA mandated to report to the EC on the changes to the reporting regime



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Changes to reporting (single-sided reporting for ETDs, intragroup exemption and “backloading”)

Single-sided reporting for ETDs

- Not included in EMIR Refit
- BUT further analysis on avoiding unnecessary duplication and simplifying reporting to be undertaken
- 18 months after entry into force – EC mandated to report on whether there is a duplicative reporting obligation under MiFIR and whether reporting of ETDs can be reduced or simplified
- 11 months after entry into force – ESMA to submit a report to the EC on consistency of reporting requirements under MiFIR and EMIR, potential alignment and on indirect client reporting

New exemption for intragroup transactions where one party is NFC or third country NFC

- Subject to certain conditions
- The relevant competent authority must be notified of the intention to rely on the exemption which will be valid unless the competent authority notifies otherwise within 3 months
- Applies immediately upon entry into force
- Within 4 years – ESMA mandated to report to the EC on the changes to the reporting regime

Removal of “backloading”

- Article 9(1) is amended to remove the requirement to report certain historic transactions
- The compliance date for “backloading” was 12 February 2019 but note ESMA forbearance statement pending finalisation of EMIR Refit
- Applies immediately upon entry into force



Clearing



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Changes to clearing (removal of frontloading, extension of pension scheme exemption, and suspension of the clearing obligation)

Removal of frontloading

- No obligation to clear OTC derivative contracts entered into or novated before the clearing obligation takes effect provided certain conditions are met
- Applies immediately upon entry into force

Extension of pension scheme exemption

- EMIR Refit extends the pension scheme exemption for at least a further two years
- Commission granted power to extend the transitional period twice for a period of one year at each extension
- Applies immediately upon entry into force (and retroactively to cover period between expiry of existing exemption in August 2018 and entry into force of EMIR Refit)
- Market participants to make best efforts to deliver technical solutions

Power to suspend the clearing obligation

- ESMA may request that the Commission suspend the clearing obligation for specific classes of OTC derivatives or for a specific type of counterparty
- May apply to counterparty or transaction types subject to conditions
- Time limited (maximum of 3 months from the date of suspension, extendable in 3 month increments up to a maximum of 12 months)
- Applies immediately upon entry into force
- No specific RTS/reports mandated
- MiFIR trading obligation may also be suspended in certain circumstances



Changes to clearing (CCP transparency)

CCP transparency of IM levels

- CCPs to provide clearing members with a simulation tool allowing them to determine on a gross basis the amount of additional IM that the CCP may require upon clearing a new transaction
- CCPs to provide clearing members with information on the IM model it uses
- Both requirements apply 6 months after entry into force



Changes to clearing (FRANDT – fair, reasonable, non-discriminatory and transparent commercial terms)

FRANDT

- Clearing members and clients of clearing members providing clearing services must do so on fair, reasonable, non-discriminatory and transparent commercial terms (although this does not amount to an obligation to contract)
- Conflicts of interest must be identified, prevented, managed and monitored

Applies 24 months after entry into force

EC empowered to adopt a delegated act specifying the conditions under which commercial terms are considered FRANDT

Within 4 years – ESMA mandated to report to the EC on the accessibility of clearing services and whether FRANDT has been effective in facilitating clearing



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Changes to clearing (bankruptcy remoteness)

Bankruptcy remoteness

- National insolvency laws should not prevent a CCP from following EMIR default procedures in respect of assets held in omnibus and individual segregated client accounts at clearing members and CCPs
- Recital indicates that indirect clients should benefit from equivalent protection

Applies 6 months after entry into force

No specific RTS/reports mandated



Risk mitigation techniques for uncleared trades



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Changes to risk mitigation techniques for uncleared trades

VM exemption – Physically settled FX forwards and swaps

- Recital 21 of EMIR Refit acknowledges the need for international regulatory convergence in respect of the VM requirements applicable to physically settled FX forwards and swaps
- Mandatory exchange of VM on physically settled FX forwards and swaps will be limited to transactions between the most systemic counterparties (i.e. credit institutions and investment firms)
- Position on IM remains unchanged

IM and VM exemption – Equity options

- Recital 21 of EMIR Refit also acknowledges the need for regulatory convergence with regard to risk management procedures for other classes of derivatives (i.e. equities)

Validation of risk management procedures for margin

- ESAs to develop RTS specifying supervisory procedures to ensure initial and ongoing validation of risk management procedures relating to collateral and segregation arrangements

IM models

- Competent authorities should validate risk management procedures plus any significant changes before they are applied



Questions?

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