European Derivative Regulation - EMIR

Frequently Asked Questions for non financial counterparties

December 2013

Contents

ACT webinars on derivative regulation have generated a large number of questions from those connected live to the broadcast. Since not all the questions posed could be answered in the time allowed those questions have been summarised here in the form of an FAQ.

The intention is to update these FAQ from time to time. December 2013 additions to the FAQ are marked **Revised** or **New.**

Further information, webinars and resources, including the **ACT briefing note European regulation of OTC derivatives: Implications for non-financial companies** are available at http://www.treasurers.org/otc

EMIR generally		
1	NFC Group question: Is there an NFC group definition for calculating clearing thresholds?	Under EMIR a non-financial counterparty NFC must calculate whether their volume of derivatives is over the set thresholds which would make them an NFC+ and subject to more onerous obligations. For threshold calculation you sum the notional amounts of all deals done by the NFC and other non-financial members of the worldwide group including intragroup deals (there is a doubling up since both ends of an internal deal must be included), HOWEVER deals that are "objectively measurable as reducing risks related to the commercial activity or treasury financing activity of the NFC or of that group" are excluded from the totals.
2	Is a non-EU company trading with a bank in EU subject to EMIR?	Any EEA bank trading derivatives will be subject to EMIR even when dealing with a non EEA company. However the non EU company is not generally bound by EU rules which means, for instance that it would not have to report the deal to a TR (Trade Repository), whereas the EU bank would. Where the non-EU company is itself subject to local laws on derivatives the outcomes are complex with rules on equivalence or substituted compliance still evolving.
3	Does this regulation cover all European countries (including CH) and inter-co transactions with non-European entities?	EMIR applies within the European Economic Area and so is not applicable in Switzerland. A similar law on market infrastructures FINFRAG is in preparation in Switzerland and is expected to come into force in 2015. An EEA party is still within scope even on inter-company and even if dealing with a non EEA party.
4	Please could you clarify the treatment of FX spots and FX forwards?	FX spot is very clearly not a derivative. FX forwards according to the European Commission are derivatives. They say "Yes; EMIR applies to all types of derivative contracts as defined in points (4) to (10) of Section C of Annex I to Directive 2004/39/EC (MIFID)." This in effect says that in order to define derivatives EMIR looks to the definitions in MiFID, but MiFID

		was a Directive so each country has implemented it in slightly different ways. In the UK case there is additional guidance from the FCA (previously FSA), and it is because of that guidance that in the UK FX done for commercial purposes rather than investment deals will not be treated by the FCA as subject to EMIR. How the borderline between these two is set remains somewhat vague, but hedging commercial purchases and sales must be commercial. Hedging debt or a new acquisition could presumably be deemed for investment purposes. However other countries in Europe probably do not have that additional guidance so for them FX forwards will be in scope for EMIR. The FCA guidance can be found by following a trail of references that starts at http://www.fca.org.uk/firms/markets/international-markets/emir/emir-library then click on the *Domestic legislation and FCA handbook*. That expands the page and go to the paragraph on *Perimeter guidance on the types of derivative covered by EMIR* then work through the PERG and RAO references.
5 **New**	I thought that hedges for commercial purposes were only excluded from the clearing calculation. Are they actually excluded from all reporting requirements?	Yes, hedges done for commercial purposes (as defined in the legislation) are not included in the clearing threshold calculation. The commercial purpose test again comes into play specifically for FX forwards and reporting in the UK as described in 4 above. In brief FX forwards done for commercial purposes do not need to be reported in the UK although they do in the rest of Europe (save for Ireland and possibly Italy).
6 **New**	FX spot deals are out of scope, but would an FX deal between a UK corporate and UK bank with a maturity date of less than spot (of two days) be reportable?	Spot deals can be for settlement anything from same day to 2 days hence, so we would interpret all such FX transactions to be out of the scope of EMIR. The transaction here is between UK entities so the treatment in 4 above is also relevant.
7 **New**	The FCA website explains the circumstances when an FX forward is not a derivative so	If the bank reports a derivative that is not strictly speaking reportable than does not mean the company has a new responsibility or obligation to

	does not fall under EMIR for UK companies. Banks intend to report all transactions as it's less complicated that way, it seems. Can you confirm that regular NFC- companies will not have to report FX forwards to a Trade Repository even if banks report their side?	report as well. Furthermore if a company decides that it will report deals that are not strictly reportable (perhaps because this avoids some administrative decisions) then by so doing the FCA will not deem that the company has in some way opted into EMIR. The other EMIR obligations will not become applicable just through this sort of voluntary reporting.
8 **New**	In a centralised cash management model, where a [UK] treasury entity may need to purchase GBP today to cure an overdraft in a GBP pooling structure, with a simultaneous sale of GBP at the end of the overdraft period, would that forward count as a commercial transaction ?	The important point to be decided here is whether the forward counts as a derivative for EMIR purposes under the UK definition of derivatives, and that hinges on whether the transaction is a commercial or investment transaction. (cf Q4 above) Were the derivative to be hedging a longer term loan, that might be treated as investment purposes, so the same could apply to an overdraft. The contrary argument would be that the overdraft is part of working capital maintained for operational trading purposes of the business and therefore might be commercial. You would be advised to seek professional legal advice on the exact circumstances applying in your company's case.
9 **New**	Is a put and call arrangement to acquire non-controlling interest of a subsidiary in scope? Does the geography of this arrangement matter?	EMIR covers derivatives as defined in MiFID Annex 1, Section C points 4 to 10. Point 4 covers options relating to securities which may be settled physically or in cash. Therefore this arrangement is subject to EMIR, as long as at least one of the parties is subject to EMIR. (Note that on 15 November 2013, ESMA published and submitted to the European Commission draft technical standards proposing that certain EMIR obligations (clearing and risk mitigation) also apply directly to EU branches of non-EU entities if they are considered to have a direct, substantial and foreseeable effect in the EU).

Reporting generally

1	When do we expect to have a registered trade repository?	The first batch of TRs were approved with effect 14th November 2013, which means the start date for reporting is 12th February 2014. See also Q10 below. **Revised**
2	How wide is the reporting requirement and will it apply to intercompany contracts eg between subsidiaries and Group Treasury.?	The reporting requirement applies to all derivatives not just OTC, so exchange traded derivative are included. Inter-company contracts are covered too with the requirement applying to both the parties involved so one inter-company deal necessitates two reports.
3	If an NFC- counterparty doesn't have the capability to report trades (FX hedges) into the repository, would that responsibility to report be on the FC (the bank)?	EMIR is clear that reporting may be delegated but that the responsibility for reporting remains with each counterparty. Thus a bank may offer a delegated reporting service and may take on certain responsibilities through a contractual service level agreement, but in law the responsibility is still with each counterparty.
4	Reporting of trades must be done daily. Which time of day (deadline); or does it matter?	Trades must be reported "no later than the working day following conclusion, modification or termination of the contract."
5	What are the sanctions for non-compliance?	Each Member State will be bringing EMIR into its normal financial regulatory provisions which may include penalties for non compliance. On the FCA website there is a statement: "If there is a reason why full compliance cannot be achieved in specific circumstances, a firm should prioritise having a detailed and realistic plan to achieve compliance within the shortest timeframe possible. However, this does not prejudge our approach to any instances of non-compliance."
6	Will there be an approved list of trade repositories and who will keep this? Where could someone access it?	The official list of registered TRs is at http://www.esma.europa.eu/page/Registered-Trade-Repositories See also Q10 below **Revised**
7	Do you have a sense of what Corporates are doing with regard to TRs? Are they signing up now - or waiting for formal	Practices within the corporate treasury community are being much debated. The impression gained by the ACT is that from around September 2013 companies were beginning to

	approval from ESMA? Or are they intending / hoping to delegate reporting to their counterparties?	make contact with potential TRs. Since mid Nov 2013 TRs are being officially approved by ESMA, so that companies should move forward with any plans to connect directly to a TR. Many companies are hoping that their banks will provide delegated reporting to take some of the burden of reporting from the companies. However not all banks have said they will offer this service and few have an actual offering ready as at September 2013. Remember too that intra-group transactions have to be reported so a direct link to a TR might be the best route to cover this. **Revised**
8	Should the derivatives be reported on a group basis? What if each subsidiary company in the Group has separate ISDA with the banks and is located in far away nations?	All derivatives done by any EEA companies within a group will have to be reported including internal transactions. These could be reported by each entity itself or perhaps if your treasury operations are centralised there may be efficiencies in having just one link to a TR at the parent level, since delegation of reporting is permitted.
9 **New**	Who can see reported trades. Is it public information?	ESMA, the European Securities and markets Authority, and other regulatory bodies will have the data available to them to enable them to fulfil their responsibilities. Data on aggregate positions by class of derivative will be made publically available but not by entity.
10 **New**	Please would you confirm who is currently registered as a trade repository	The registrations of the first Trade Repositories were approved by ESMA with effect 14th November 2013 and were: • DTCC Derivatives Repository Ltd. (DDRL), based in the United Kingdom; • Krajowy Depozyt Papierów Wartosciowych S.A. (KDPW), based in Poland; • Regis-TR S.A., based in Luxembourg; and • UnaVista Ltd, based in the United Kingdom. On 28th Nov 2013 ESMA approved the registrations of two further TRs namely: • ICE Trade Vault Europe Ltd. UK based; and • CME Trade Repository Ltd. UK based

11 **New**	If we have an internal deal with a legal entity outside the EU how do we report this?	The EEA based entity will have to report the transaction. Within the counterparty data section there is a field to be reported specifying whether the trade is with a non-EEA counterparty - Yes or No.
12 **New**	Please could you clarify when trades entered into after 16th August 2012 need to be reported. Is it the same for those that have matured before 12th February 2014 and/or will mature after 12th February 2014?	Derivatives outstanding on 16th August 2012, or entered into after that date but no longer outstanding on the reporting start date of 12 February 2014 must be reported within 3 years of 12 Feb 2013. Derivatives outstanding on 16th August 2012 and still outstanding on the reporting start date (12 Feb 2014) must be reported within 90 days of the reporting start date. For derivatives dealt since 16th August 2012 and still outstanding on the reporting start date (12 Feb 2014) there has been some lack of clarity since the transition rules in the regulatory technical standards are silent on the matter. This means that the deals in this category simply have to be reported by the normal Reporting Start Date ie by 12 Feb 2014. **Revised 23.12.13**
13 **New**	I heard that valuation field would not initially be required in Feb 2014 but only after 180 days. Is this true?	The ESMA Q&A at http://www.esma.europa.eu/system/files/2013-1633_qa_iv_on_emir_implementation_0.pdf explain at answer TR 3 b that "The reporting start date is extended by 180 days for the reporting of information referred to in Article 3 of Regulation (EU) 148/2013, i.e. data on exposure. The corresponding fields in the table are the fields related to valuation and collateral (fields 17 to 26 of Table 1)." But remember that an NFC- is not required to report valuations, even after the 180 days.
14 **New**	Do you register with one Trade Repository only? If a bank reports a trade on your behalf do they need to report to your TR if their TR is different or can they report both sides of the trade to their TR?	A company may decide to register with more than one trade repository, although you would expect it to be more efficient and cost effective to use just one. If the company delegates its reporting to its bank then that bank may well report the transactions to a different TR. There is no need for the company and the bank to be using the same TR.

15 **New**	Corporates are typically using derivatives to hedge some business activity, yet the reporting can't evidence this due to the limited & fragmented scope of products to be reported eg bonds are not reported when issued by companies. How will FCA avoid chasing false positives which suggest a corporate has a huge naked IRS which is actually just a hedge?	From a regulatory review standpoint yes the repository data could show a company with a large naked derivative exposure. Regulators will be concerned about build up of risk in the non-financial side if material. They may be prompted to make enquiries, at which stage they will need to understand if there is some counterbalancing business exposure.
16 **New**	We work with US counterparties that are already reporting under Dodd Frank requirements. Do we have to report under both DF and EMIR ?	Dodd Frank allows for one sided reporting by the financial party, whereas in Europe both sides must report. As the non financial side to a transaction it is unlikely that you will have to report under DF and EMIR although it is possible that in a given transaction one side may report under EMIR while the other side reports under DF. One of the fields to be reported under EMIR is to state whether the counterparty is in the EEA – yes or no. In other words this flags that the EMIR reporting will be one-sided.
17 **New**	Do the trade repositories provide a template for sending them the data? For example as a csv?	Yes it is expected that the TRs will be providing suitable templates.
18 **New**	My Singaporean entity has entered into a derivative contract with another group entity based in Australia. My understanding is there are no reporting obligations from ESMA for both entities even though parent company of both entities is a UK plc?	Your interpretation is correct. EMIR is only applicable where at least one side to the transaction is an EEA undertaking. (There are remote exceptions for example where there are two third country entities, i.e. non EEA, where the contract has a "direct, substantial and foreseeable effect within the Union".)
19 **New**	For intra group transactions, how do other subs nominate Group Treasury to report on their behalf (template letter?) and to whom do they send this	For internal purposes it would be good practice to have a formal agreement that Group treasury is to undertake the reporting for a given subsidiary, to specify the service standards required and to clarify the legal responsibilities and liabilities between the parties.

	nomination?	As far as the outside world is concerned it will be a matter of fact if group treasury is reporting on behalf of a subsidiary as well as itself. This will become apparent from the completion of the field for reporting entity ID, namely the party to whom the reporting has been delegated, and which is otherwise left blank.
20 **New**	I am a UK plc who has an IRS with an American Bank with a UK branch. This bank tells me that they are not subject to EMIR and that the IRS does not require to be reported. Is this correct?	The EMIR reporting obligation applies to all banks authorised under the EU Capital Requirements Directive (amongst other entities). In the case of the UK branch, the legal entity involved is the American Bank which is not within the scope of the EMIR reporting obligation. However, that does not remove the obligation for the UK plc to report its own counterparty data and the common data in respect of the transaction. The UK plc will also need to identify the non-EU counterparty in its report (ESMA Q&As (TR Question 15)).
21 **New**	If a U.S. based group treasury function executes forward currency trades directly for their European subsidiary (that is, the actual trade ticket shows the deal between European Subsidiary XYZ and Bank ABC), is the U.S. based company required to comply with the EMIR reporting?	The US treasury function is in effect acting as the agent of the European subsidiary so that subsidiary is the legal entity that is counterparty to the derivative. The European subsidiary will therefore have to comply with the EMIR reporting obligation, but it can delegate all or part of the administrative process of reporting to its US treasury if it so wishes (in which case the European subsidiary must have the ability to audit any reports made on its behalf in order to confirm that they are accurate).

Reconciliations and protocols

1	Should firms sign up to the ISDA protocol or to the bilateral sent by banks, please?	The ISDA protocol is a convenient method for amending all your ISDA agreements with all your banks via a single adherence letter, and many companies are doing so. The downside is you have to agree to every

		bit of it with no amendments. We understand that banks are seeking agreement from the customers to bilateral arrangements that are very similar in structure to the ISDA protocol, but presumably there would be more scope to tailor these procedures. If the customer agrees to be a receiving party under the ISDA protocol there is a presumption that the customer agrees the reconciliation if they do not reply within 5 days. Performing the reconciliations for many will take longer than this so companies must be alert that through neglect or delay they do not inadvertently agree to position data that is wrong.
2	Some of our bank counterparties have suggested they cannot trade with us unless we adhere to the EMIR protocols by 15 September 2013. Please can you shed some light on the matter?	With effect from 15th September 2013 the EMIR obligation to have agreed reconciliation and disputes arrangements in place between counterparties comes into force. These arrangements must be agreed in writing. Whether you agree on a bilateral basis or through signing up to the ISDA protocol is for you and your counterparties to agree. Many companies are finding that the protocol route is a convenient way of dealing with many counterparties through one document. However if signing up as a receiving party you need to be sure that you will be able to review and reconcile the data you receive within the 5 days or at least be ready to respond.
3	Does an NFC- entity require an LEI in order to be able to adhere to the NFC Representation Protocol?	When signing up for the ISDA 2013 EMIR Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol (http://www2.isda.org/functional-areas/protocol-management/open-protocols) the form for adherence does ask for an LEI (Legal Entity Identifier) but this field is not mandatory so you can sign up even without first having an LEI.
4	When registering for the ISDA protocol should only the treasury company within a group in a group that executes external derivatives register only?	All parties that transact derivatives must have agreed in writing to arrangements for reconciliations and dealing with disputes. So each group company dealing externally will need to do something, however you can choose whether to make arrangements bilaterally with your banks or to do it "in bulk" with each group company signing up to adherence to the protocol. Bear in mind that if two group companies sign up to the protocol as receivers they have effectively agreed with each other to both be receivers, which obviously does not work.

		Within groups treasurers are often dealing with the requirement to have reconciliation and dispute procedures in place internally through amending group manuals / procedures.
5 **New**	Portfolio Reconciliation: how can a NFC- reconcile annually when the bank needs to reconcile more frequently?	The regulatory technical standards do allow various concessions so that an NFC- need not reconcile as frequently as is required for an FC or NFC+. It would be illogical to allow a concession and then make it ineffective by requiring the rules for the FC to apply, therefore we must assume that the rules for the NFC- party prevail.
6 **New**	Resolution of OTC valuation discrepancies. So far, every time we raise a valuation discrepancy with a counterparty, we receive the same response claiming that they confirm their valuations and cannot disclose their pricing methods as they are considered proprietary information. On this basis discrepancies cannot be resolved. Is there a plan under EMIR to provide more specific guidelines on what information have to be exchanged between counterparties to resolve such discrepancies?	EMIR requires counterparties entering into an OTC derivatives contract to perform regular portfolio reconciliations and both counterparties to that contract are legally responsible for compliance with the portfolio reconciliation obligation. The ESMA Q&As (OTC Question 15) recognise that counterparties may agree up front that discrepancies relating to the recognition or valuation of a contract and to the exchange of collateral that amount to a value below a pre-defined threshold do not count as disputes. Therefore, if you have such an agreement in place with your counterparties, only discrepancies in respect of amounts above the agreed pre-defined threshold would count as disputes and be treated according to Article 15 of the EMIR OTC technical standards. An NFC-is not required to reconcile valuations.
7 **New**	We work with a local Swiss bank (Banque cantonale) who is saying that since they are Swiss they are not obliged yet to report. How can we perform the reconciliation ?	A Swiss bank is not subject to the EMIR reporting obligation or the EMIR portfolio reconciliation obligation (but Switzerland has indicated that they expect to enact similar rules). However, as EMIR requires EU counterparties to agree portfolio reconciliation arrangements and perform such arrangements with their counterparties (regardless of whether their counterparties are themselves subject to EMIR), in order to fulfil your own EMIR portfolio compression obligations you will need to reach a contractual agreement for your Swiss bank to co-operate (and therefore, in effect, for your Swiss bank to comply with the EMIR portfolio reconciliation

		requirements even though it is not technically subject to them).

LEI – Legal Entity Identifiers

1	How do we obtain an LEI	Companies will have to apply for a Legal Entity Identifier(LEI) , but as yet the final system for creating these reference numbers does not exist. Instead pre-LEIs are being generated by pre-Local Operating Units (pre-LOU) such as the Irish Stock Exchange, the London Stock Exchange (Una Vista), WM Datenservice based in Germany and the established CICI in the US (cf www.leiroc.org). The term International Entity Identifier (IEE) is sometimes used interchangeably with LEI. The endorsed Pre-LOUs of the Interim Global Legal Entity Identifier System as at December 2013 are at http://www.leiroc.org/publications/gls/lou_20131003_2.pdf
2	LEI - which entities need to be registered - just the parent co or each subsidiary entity that may be a party to a derivatives trade.	Every single entity dealing in derivatives, including intra group transactions will need its own LEI. Some of the LEI issuing bodies will be catering for a bulk upload of group entities.
3	Have most NFC-companies already obtained LEI?	As of September 2013 most companies have not yet embarked on the process of obtaining an LEI. Ahead of the deadline for starting trade reporting the issuing bodies, the pre Local Operating Units, could be subject to a rush to apply. To be on the safe side an early application is recommended.
4	Does the CICI suffice as LEI?	Yes. Although the CICI is issued by an American body it is nonetheless suitable for use in Europe for EMIR reporting purposes.
5	Is there a deadline around obtaining LEIs?	LEIs will be required in time for the reporting start date which is 12th February 2014.

6 **New**	Is CICI Code obtained under Dodd Frank accepted as LEI or do we in some way have to port it to the LSE?	An LEI issued by CICI is suitable for use in Europe under EMIR.
7 **New**	What is the difference between LEIROC and CICI ?	LEIROC is the Legal Entity Identifier Regulatory Oversight Committee which is committee of authorities from around the world working to coordinate and oversee a global system of legal entity identification. CICI utility is one of the Pre-LOUs of the Interim Global Legal Entity Identifier System approved by LEIROC. http://www.esma.europa.eu/system/files/2013-1633_qa_iv_on_emir_implementation_0.pdf answer TR 10b explains that for EMIR the LEI has to be issued by one of the endorsed pre-LOUs at http://www.leiroc.org/publications/gls/lou_20131003_2.pdf

UTI – Unique Trade Identifiers

1	Do Corporate and banks have to agree UTI standards bilaterally? Is there any industry wide approach available?	The UTI or Unique Transaction Identifier has to be unique and specific to each and every transaction. Both parties to a transaction must obviously be using the same UTI. As of September 2013 there is no internationally agreed or recommended UTI but various ideas and precedents are developing, notably with ISDA taking a lead. If one party creates a UTI made up of its own LEI or company name combined with a reference that it generates uniquely then there is a good chance that it will also be unique as regards the wider world. The eventual system may well work on some hierarchy as to which party will take responsibility for generating a UTI, starting with the exchange for exchange traded deals, the platform provider, the confirmations matching provider or down to the financial party for OTC non electronically confirmed deals or based on alphabetic order as a tie breaker if needed.

		If no recognised market practice develops then on every transaction it will be up to the parties to agree a suitable UTI. ESMA is expected to issue some guidance but as of early December 2013 this has not yet happened.
2 **New**	How would we get a UTI on deals that have been entered into before the EMIR regulation was in force? According to EMIR we have to back report deals from August 2012, but we would not have an UTI for those deals.	Yes old deals outstanding since 16th August 2012 or executed since then will need to be reported and therefore a UTI will be required. The same process for allocating a UTI on a current deal could be employed, in other words the NFC will typically rely on its bank counterparty to generate the UTI. But going over the back book and matching up all the deals recorded by the NFC with those recorded by the bank is a major task. Internal deals since 16th August 2012 will also need to be allocated a UTI.
3 **New**	Fine to say that a corporate can get a UTI from the bank, but how do you get a UTI for an intercompany deal?	As with any UTI it will be the parties involved to agree a UTI and make sure they are both using the same reference for the same deal. For example if one party creates a UTI made up of its own LEI combined with a reference that it generates uniquely then there is a good chance that it will also be unique as regards the wider world. However once ESMA has issued its guidance companies will be expected to use that common model for UTI generation.