



April 2019

EMIR 2.1 update

In July 2018 we circulated a client briefing note outlining the European Parliament's approval of a revised proposal to amend EMIR (also known as "**EMIR 2.1**") (the "**EMIR 2.1 Note**", which can be found [here](#)). This briefing note outlines a development that has occurred in respect of EMIR 2.1.

On 28 March 2019, the European Securities and Markets Authority ("**ESMA**") published a statement (the "**ESMA Statement**") on the implementation of the new clearing obligation regime for financial counterparties ("**FCs**") and non-financial counterparties ("**NFCs**") under EMIR 2.1.

The ESMA Statement is particularly important for:

- FCs who wish to benefit from the exemptions granted to small financial counterparties ("**SFCs**"); and
- NFCs who are required to determine whether they are an NFC+ and therefore subject to more onerous requirements under EMIR.

IMPACT OF THE ESMA STATEMENT

The ESMA Statement confirms that both FCs and NFCs should start calculating their relevant aggregate month-end average notional position of outstanding OTC derivatives transactions over the previous 12 months. This calculation will enable such entities to determine whether they are above or below the 'clearing thresholds' (summarised below) and, thus, whether they will be subject to the clearing obligation under EMIR 2.1.

Should an FC or NFC exceed any of the clearing thresholds, it must notify its relevant National Competent Authority ("**NCA**") and ESMA on the day EMIR 2.1 enters into force, which in ESMA's view could be as early as the end of May 2019.

NFCs and FCs can choose whether or not to conduct this calculation. However, electing *not* to perform this calculation will result in the entity being subject to the clearing obligation in respect of all asset classes of OTC derivatives transactions.

This means that for an FC or NFC that either:

- exceeds any of the clearing thresholds; or
- chooses not to conduct the calculation,

it will be required immediately to notify both its NCA (in the case of an entity established in the UK, the FCA) and ESMA on the day EMIR 2.1 enters into force.

On 2 April, the FCA issued a notification to the market (the "**FCA Notification**") clarifying that it will require both FCs and NFCs (that are established in the UK) taking positions in OTC derivatives transactions and choosing to conduct the calculation of their aggregate month-end positions to start preparing for such calculation, in order to be ready to notify the FCA (and ESMA) on the day EMIR 2.1 enters into force. The FCA has stated that it is in the process of updating its 'EMIR Notifications Web Portal' so that it will be able to accept such notifications via its online platform.

Broad overview of the calculation to be conducted under EMIR 2.1

Scope: each NFC and FC to calculate the aggregate month-end average notional position of outstanding OTC derivatives for the previous 12 months. This calculation is generally to be conducted on a **group-wide basis**. However, where the FC is an AIF or a UCITS, the calculation should be conducted at fund level.¹

When conducting the calculation, an NFC will only look at non risk-reducing OTC derivatives transactions entered into by that NFC (and all other NFCs within its group), whereas an FC must include all OTC derivatives transactions (regardless of whether they are risk-reducing transactions) entered into by that FC (and all other entities within its group where applicable, noting the exception for an AIF or a UCITS outlined above).

Clearing thresholds (in each case gross notional value):

- OTC credit derivatives: €1 billion
- OTC equity derivatives: €1 billion
- OTC interest rate derivatives: €3 billion
- OTC foreign exchange derivatives: €3 billion
- OTC commodity derivatives and other OTC derivatives not listed above: €3 billion

NFCs

Broadly, to the extent an NFC's calculation exceeds any of the above clearing thresholds, it will be treated as an "NFC+" in respect of that asset class and will therefore be subject to the clearing requirement for transactions of that asset class only. However, it is important to highlight that, where an NFC+ exceeds the clearing threshold in respect of one asset class, the requirement for that NFC+ to post margin will thereafter apply in respect of transactions in all asset classes and not just its transactions of that specific asset class.

FCs

Exceeding of the clearing threshold for at least one asset class by an FC will trigger the clearing obligation in respect of all asset classes entered into by that FC.

Only where an FC's calculation is below all the clearing thresholds, will it be treated as an SFC and will therefore be exempt from the clearing requirement (but not the margin requirement) once EMIR 2.1 takes effect.

¹ However, an AIFM or UCITS Management Company which manages more than one AIF or UCITS, as applicable, must "be able to demonstrate to the relevant competent authority that the calculation of positions at the fund level does not lead to: (i) a systematic underestimation of the positions of any of the funds they manage or the positions of the manager; and (ii) a circumvention of the clearing obligation".

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OTHER RELEVANT FACTORS

Definition of "Financial Counterparty"

Our EMIR 2.1 Note also highlighted the broadening of the definition of FCs under EMIR 2.1. Certain industry bodies have since taken the view that, under EMIR 2.1, **non-EEA AIFs managed by non-EEA AIFMs** will remain third-country entities (for EMIR purposes). However, when transacting with an EEA broker/bank, they *may* be treated by that EEA broker/bank as a **deemed FC rather than a deemed NFC**. As a result these entities might become subject to the more onerous obligations under EMIR (e.g. the mandatory margin requirement (to exchange collateral) and the clearing requirement, in each case in respect of certain in-scope derivatives transactions). However, a market consensus has not been reached on this point, so it remains unclear how these entities will be treated for EMIR-compliance purposes when transacting with an EEA broker/bank.

Brexit

The implementation of EMIR 2.1 into UK law, and its eventual operation, is still subject to further clarity in respect of Brexit. Please refer to our [January 2019 note on UKMIR](#) for further discussion of the "onshoring" of EMIR into UK law in the event of a no-deal Brexit.

CONCLUSION

Whilst the implementation date of EMIR 2.1 has not yet been finalised and there could therefore be further developments before EMIR 2.1 enters into force, the ESMA Statement and the FCA Notification provide welcome guidance for FCs and NFCs.

Should you have any questions in relation to this email, please contact one of the Derivatives & Structured Products team, or your usual Travers Smith contact.

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