

Reporting of OTC Derivatives Between FC and NFC- Entities After 18 June 2020

EMIR REFIT Mandatory Reporting provisions require market participants to consider their existing Delegated Reporting arrangements.

Key Points:

- From 18 June 2020, financial counterparties (FCs) will be liable for the timely and accurate reporting of over-the-counter (OTC) derivative contracts on behalf of both themselves and their non-financial counterparties (NFCs) that are not subject to the clearing obligation (NFC-s) (Mandatory Reporting). To enable an FC to report, an NFC- will need to provide to such FC the data that the FC cannot reasonably be expected to possess. Currently the obligation to report applies to both parties, with NFC-s often delegating their reporting obligations to FCs or third parties (Delegated Reporting).
- An NFC- will remain liable to report OTC derivative contracts entered into with a third-country counterparty that would be an FC if it were established in the EU (TCE FC), unless such third-country reporting legal regime has been declared equivalent to EMIR and such TCE FC reports OTC derivative contracts to a trade repository (TR) in accordance with such regime. There is currently no such regime.
- Mandatory Reporting applies only to OTC derivative contracts and NFC-s will remain liable for reporting their exchange traded derivative contracts entered into with an FC, even when an NFC- has delegated such reporting to an FC.
- On 26 March 2020, the European Securities and Market Authority (ESMA) published a consultation paper setting out the arrangements that it proposes to implement in connection with Mandatory Reporting.
- The existing delegated reporting arrangements between NFC- and FC entities will need to be reviewed in light of Mandatory Reporting and the proposals in the consultation paper.
- From 17 June 2019, the EMIR REFIT introduced an exemption for reporting intragroup derivative contracts provided that certain conditions are satisfied.

Pursuant to Article 9 of the [European Market Infrastructure Regulation \(EU\) 648/2012](#) (EMIR) counterparties to derivative contracts are required to provide details of any concluded OTC and exchange traded contracts (including any modifications or termination of such contracts) to a TR registered with ESMA, by the following business day (T+1). [Regulation \(EU\) 2019/834](#) (EMIR REFIT), that came into force on 17 June 2019 and amended EMIR, reduces the burden of reporting OTC derivative contracts for NFC-s.

Mandatory Reporting

From 18 June 2020, FCs will be solely responsible and legally liable for: (i) reporting to a trade repository on behalf of both counterparties the details of OTC derivative contracts concluded with an NFC-; and (ii) ensuring the correctness of the details reported. Mandatory Reporting will not apply if an NFC- chooses to report for itself and informs the FC accordingly. NFC- entities that invested in a reporting system may decide to use this option, particularly if they are likely to cross the clearing threshold from time to time (at which point Mandatory Reporting ceases to apply).

When entering into OTC derivative contracts with a TCE FC, an NFC- will not need to report if the following conditions are satisfied:

- The legal regime for reporting to which the TCE FC is subject has been declared equivalent pursuant to Article 13 of EMIR.
- The TCE FC has reported OTC derivative transactions pursuant to that third country's legal regime for reporting to a TR, and the relevant TR is subject to a legally binding and enforceable obligation to grant the entities referred to in Article 81(3) of EMIR direct and immediate access to the data.

As of the date of this update, [no equivalence decision](#) regarding the reporting obligation has been reached with respect to any other legal regime.

Pursuant to the reporting regime currently applicable under EMIR, each party to an OTC derivative contract (including an NFC-) is independently responsible for ensuring reporting is carried out. In practice, NFC-s often delegate their reporting obligation to FCs (or third parties) who report on their behalf. Delegated Reporting does not transfer the allocation of responsibility, which ultimately remains with the relevant NFC-, however, from 18 June 2020, Mandatory Reporting changes the current position and places the reporting responsibility on an FC.

Mandatory Reporting requirement applies to OTC derivative contracts (as defined in EMIR¹, *i.e.*, derivatives not executed on a regulated market or on a third-country market considered as equivalent to a regulated market) and NFC-s will remain liable for reporting their exchange traded derivative contracts concluded on a regulated market or on a third-country market considered as equivalent to a regulated market. This means that NFC-s may need to adopt different approaches to reporting their OTC derivative contracts and their exchange traded derivative contracts.

Intragroup Transactions Reporting

From 17 June 2019, the EMIR REFIT reduced the regulatory burden on corporate groups, meaning intragroup derivative contracts involving at least one NFC (or an entity that would be qualified as an NFC if it were established in the EU) no longer need to be reported provided that:

- Both parties are included in the same consolidation on a full basis
- Both parties are subject to appropriate centralised risk evaluation, measurement, and control procedures
- Their parent undertaking is not an FC

In order to disapply the application of the reporting obligations to intragroup derivative contracts, counterparties will need to notify relevant competent authorities of their intention to apply this exemption. Counterparties may rely on the exemption once all relevant competent authorities have either confirmed the conditions are satisfied or, if no response is received, three months following the notifications.

ESMA Consultation

The EMIR REFIT enables ESMA to review and develop technical standards for EMIR reporting. On 26 March 2020, ESMA published a [consultation paper](#) setting out the draft Regulatory Technical Standards and Implementing Technical Standards (RTS and ITS) under the EMIR REFIT that deal with reporting to TRs, procedures to reconcile and validate the data, and data access by the relevant authorities and registration of the TRs (the ESMA Consultation Paper). Amongst other measures, ESMA proposed to revise certain aspects of reporting to the TRs in order to align the reporting requirements in the EU with the global guidance issued by the Committee on Payments and Market Infrastructure and the International Organization of Securities Commission working group for the harmonisation of key OTC derivatives data elements.

The ESMA Consultation Paper includes draft ITS that require an FC liable for Mandatory Reporting to implement at least the following arrangements to ensure the correct reporting of derivative transactions:

- Arrangements to ensure timely provision by the NFC- of the following details of the OTC derivative contracts that the FC cannot reasonably be expected to possess:
 - Broker ID (if unknown by the FC)
 - Clearing Member (if unknown by the FC)
 - Type of ID of the beneficiary (if different from the NFC-)
 - Beneficiary ID (if different from the NFC-)
 - Whether the relevant transaction is directly linked to commercial activity or treasury financing
- Arrangements requiring the NFC to inform the FC of any change in its classification for EMIR purposes (in writing or other equivalent electronic means with at least five working days' notice)
- Arrangements obliging the NFC to maintain and duly renew its Legal Entity Identifier
- Arrangements to ensure timely notification by the NFC to the FC of its decision to start or to cease reporting the details of OTC derivative contracts (in writing or other equivalent electronic means with at least five working days' notice)
- Arrangements specifying which derivative contracts shall be reported by each of the two counterparties, if the NFC- decides to report the details of only some of the OTC derivative contracts concluded with the FC

The ESMA Consultation Paper further clarifies that Mandatory Reporting applies not only to new OTC derivative transactions concluded between NFC-s and FCs after 18 June 2020, but also to the modifications or terminations of OTC derivative contracts existing prior to 18 June 2020 (unless the parties contractually agree that the responsibility of the FC will be limited to the new OTC derivative contracts only). If an FC and an NFC- report to two different TRs, the NFC- will either need to transfer outstanding derivatives to the TR of the FC or, alternatively, the FC may decide to become a client of the TR of the NFC-, in each case, prior to 18 June 2020.

In addition, the ESMA Consultation Paper clarifies that, if (i) an NFC does not calculate its positions; or (ii) following the annual reassessment of the NFC-s derivative contracts positions against the clearing thresholds (pursuant to Article 10 of EMIR, as amended by the EMIR REFIT), the NFC exceeds one of the clearing thresholds (thus becoming an "NFC+"), in each such case Mandatory Reporting ceases to apply and an NFC becomes responsible for the reporting of OTC derivative transactions.

The closing date for responses to the consultation is 19 June 2020.

Next Steps

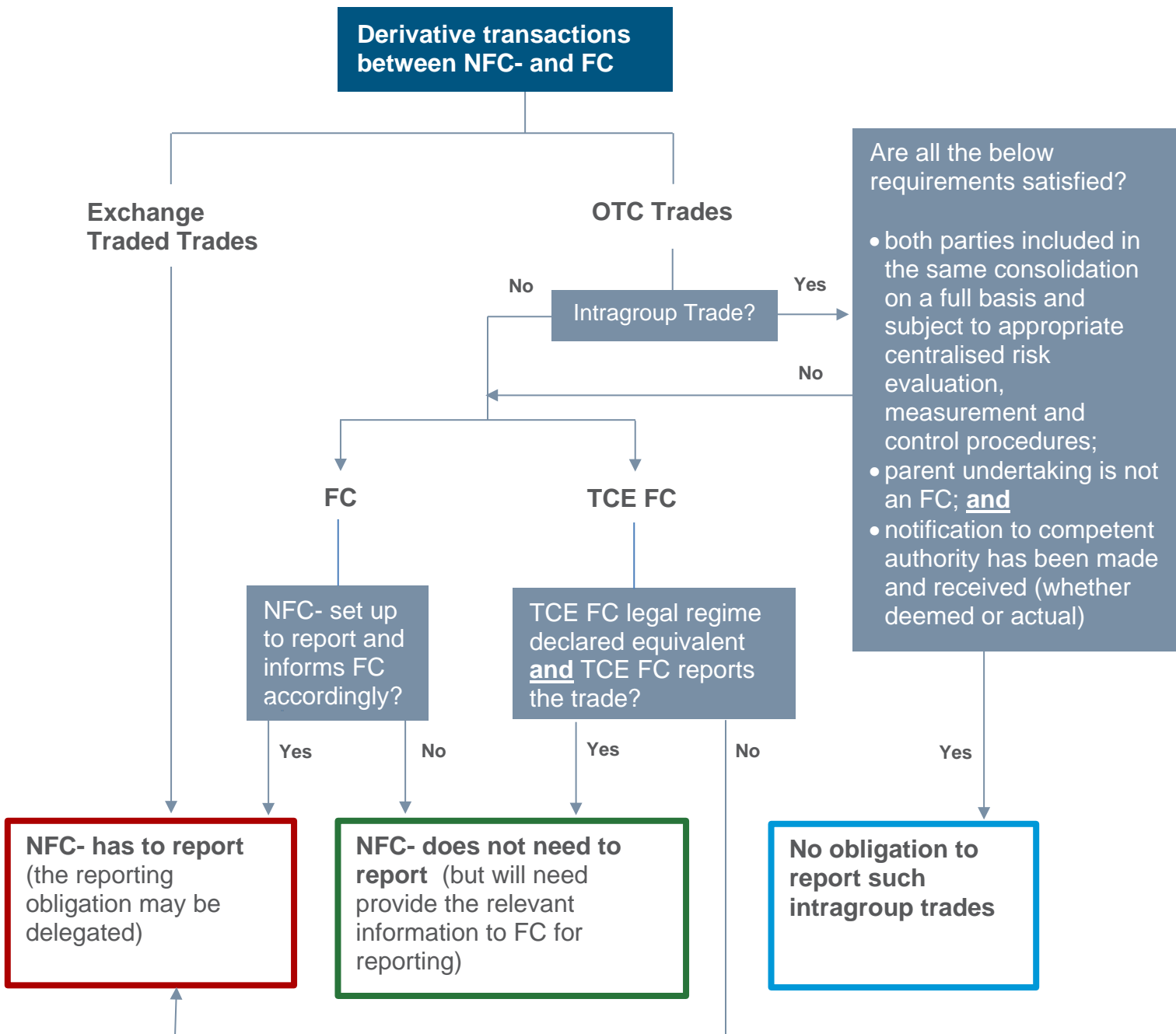
Given the application of Mandatory Reporting from 18 June 2020, NFC-s may want to consider amending or terminating their existing delegated reporting arrangements with FCs.

In December 2019, the International Swaps and Derivatives Association, Inc. (ISDA), in association with other industry bodies, published the Master Regulatory Reporting Agreement (MRRA) to replace the previously published ISDA/FIA Form of Delegated Reporting Agreement. The MRRA was drafted to work with the amendments introduced by the EMIR REFIT and sets out elective provisions governing both Mandatory Reporting and Delegated Reporting of derivative transactions for EMIR purposes. In addition, the provisions included in the MRRA are intended to ensure that its terms remain effective post-Brexit.

In order to ensure that FCs have all the required data to fulfill Mandatory Reporting, the EMIR REFIT obliges NFC-s to provide to FCs the limited details relating to the OTC derivative contracts that FCs cannot be reasonably expected to possess. Unless the existing delegated reporting arrangements are replaced with an MRRA, FCs are likely to require NFC-s to enter into new contractual arrangements on terms similar to Mandatory Reporting provisions found in the MRRA. Such new arrangements will require NFC-s to provide the relevant information, including the details referred to in the ESMA Consultation Paper. These contractual arrangements should be carefully reviewed to ensure that an NFC- does not confirm an opt out (actual or deemed) from the application of Mandatory Reporting if such NFC- does not intend to be responsible for reporting going forward.

When dealing with third-country FCs, NFC- entities will need either to report their OTC derivative contracts entered into with TCE FCs or enter into Delegated Reporting arrangements.

Does NFC- EMIR reporting obligation arise when dealing with an FC/TCE FC after 18 June 2020?



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Endnotes

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- ¹ Article 2(7) of EMIR defines OTC derivative contract as a derivative contract the execution of which does not take place on a regulated market as within the meaning of Article 4(1)(14) of Directive 2004/39/EC or on a third-country market considered as equivalent to a regulated market in accordance with Article 19(6) of Directive 2004/39/EC.