ISDA. Safe, Efficient Markets

# Explanatory memorandum to the ISDA Master Regulatory Disclosure Letter

**Dated 7 June 2019**

**International Swaps and Derivatives Association, Inc.** ("**ISDA**") has prepared this explanatory memorandum to assist in your consideration of the form of the ISDA Master Regulatory Disclosure Letter published by ISDA on 7 June 2019 (the "**Master Regulatory Disclosure Letter**").

***THIS EXPLANATORY MEMORANDUM DOES NOT PURPORT TO BE AND SHOULD NOT BE CONSIDERED A GUIDE TO OR AN EXPLANATION OF ALL RELEVANT ISSUES OR CONSIDERATIONS IN CONNECTION WITH THE MASTER REGULATORY DISCLOSURE LETTER OR COMPLIANCE WITH THE REGULATIONS OR LAWS DETAILED IN ANY OF THE APPENDICES TO THE MASTER REGULATORY DISCLOSURE LETTER. PARTIES SHOULD CONSULT WITH THEIR LEGAL ADVISERS AND ANY OTHER ADVISER THEY DEEM APPROPRIATE PRIOR TO USING THE MASTER REGULATORY DISCLOSURE LETTER. ISDA ASSUMES NO RESPONSIBILITY FOR ANY USE TO WHICH ANY OF ITS DOCUMENTATION OR OTHER DOCUMENTATION MAY BE PUT.***

## INTRODUCTION

The Master Regulatory Disclosure Letter is a form of letter that market participants may find useful as part of the management of their regulatory obligations under the laws of the jurisdictions to which the applicable appendices (each, an "**Appendix**" and together the "**Appendices**") relate, in regard to clearing over-the-counter ("**OTC**") derivatives, mitigation of risks associated with uncleared OTC derivatives, reporting of derivatives transactions to trade repositories, and associated obligations.

The Master Regulatory Disclosure Letter is a method of communicating classification status between counterparties to enable the recipient of the Master Regulatory Disclosure Letter to determine the application of certain regulatory requirements. By answering a series of questions in one or more of the Appendices to the Master Regulatory Disclosure Letter, derivatives counterparties can classify themselves according to the relevant taxonomy in the jurisdiction(s) in which they trade derivatives and to which the applicable Appendix(ces) relate(s). Where regulatory obligations depend on the classification of *both* parties to a given transaction, each party as the "**Named Entity**" would deliver a completed copy of the Master Regulatory Disclosure Letter to the other party as the "**Recipient**".

As at 7 June 2019, Appendix A (*European Union*) relating to the regulatory obligations of market participants in respect of EMIR has been published. Whilst Appendix A (*European Union*) contains a number of new questions, it also consolidates content previously published as part of other ISDA documentation, including the ISDA EMIR Classification Letter published by ISDA on 13 July 2015 and as updated and further published on 13 April 2016, the ISDA 2013 EMIR NFC Representation Protocol published by ISDA on 8 March 2013 and the ISDA Regulatory Margin Self-Disclosure Letter published by ISDA on 30 June 2016. Appendix A (*European Union*) contains transitional provisions to address the interaction between Appendix A (*European Union*) and those existing documents.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

The Master Regulatory Disclosure Letter has been developed as a bilateral version of a corresponding ISDA Amend tool for use by parties which do not subscribe to ISDA Amend or prefer to use a paper-based solution. To help ensure conformity where a party receives classification information from both the Master Regulatory Disclosure Letter and ISDA Amend, the questions and answers in the Master Regulatory Disclosure Letter mirror those used on ISDA Amend. It should also be noted that this guidance follows very closely the guidance which is available for users of ISDA Amend.

## GUIDANCE TO THE MASTER REGULATORY DISCLOSURE LETTER

The expectation is that entities will complete each relevant Appendix, in consultation with the intended recipient if required, and deliver both (i) the Appendix(ces) and (ii) the executed main body of the Master Regulatory Disclosure Letter to the relevant recipient.

Following initial delivery of the Master Regulatory Disclosure Letter to a recipient, an entity may deliver a new Appendix or a revised version of an existing Appendix. To do so, the relevant entity should re-execute and deliver the Master Regulatory Disclosure Letter *and* append any Appendix, previously delivered or new, which it seeks to utilise going forward. Entities should note that the Master Regulatory Disclosure Letter provides that, where an entity subsequently delivers a revised version of the Master Regulatory Disclosure Letter but fails to attach all previously delivered Appendices, any such Appendix will be deemed redelivered in its previously delivered form unless an express statement is made to the contrary. If an entity wishes to withdraw the statements it has made in a previously delivered Appendix or otherwise cease to make them, it should notify each recipient of this expressly; failing to redeliver a previously delivered Appendix will not be sufficient.

Pursuant to paragraph B (*Reliance*) of the main body of the Master Regulatory Disclosure Letter, the Named Entity commits to notify the Recipient in writing before, or as soon as reasonably practicable following, any of the statements made by it in any Appendix ceasing to be true. Until such notification is given to it, the Recipient may continue to rely on the statements provided by the Named Entity. The intention is that, at any point in time, the most recent communication between the Named Entity and the Recipient in relation to the Master Regulatory Disclosure Letter shall prevail, irrespective of whether that communication is made via the paper-based solution or ISDA Amend (or an equivalent electronic platform, as applicable).

A standard signature block is included but, as stated in the footnotes, this may need to be amended in some cases, such as where an agent or manager is acting on behalf of one or more clients or funds.

It should also be noted that, while the Master Regulatory Disclosure Letter is drafted in the form of a letter, a Named Entity may choose to deliver the Master Regulatory Disclosure Letter and the statements therein by way of attachment to an email or by another method of written communication, as and to the extent permitted in the relevant jurisdiction.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

**CONTENTS**

GUIDANCE TO APPENDIX A (EUROPEAN UNION) ........................................................4



Copyright © 2019 by International Swaps and Derivatives Association, Inc.

## GUIDANCE TO APPENDIX A (EUROPEAN UNION)

### WHY THE DATA IS NEEDED

#### General Introduction

EMIR is a European Union ("**EU**") regulation that deals principally with clearing OTC derivatives, mitigation of risks associated with uncleared OTC derivatives through mechanisms such as the exchange of collateral, and reporting of derivatives transactions to trade repositories.

The application of the EMIR obligations mentioned above to a given entity – both in terms of whether the obligations apply and, if so, the extent to which they apply – depends on, among other things, how that entity is classified according to the taxonomy used in EMIR.

- As a preliminary matter, certain specified types of entity are wholly exempt from the obligations in EMIR; certain other specified types of entity are exempt in part. In general terms, these include (among other entities) certain central banks, public authorities, multilateral development banks and other supranational bodies.
- For entities that are not expressly exempted, EMIR distinguishes between:
  - "financial counterparties" ("**FCs**") – in general terms, entities authorised under one of a number of pieces of EU financial services legislation;
  - "non-financial counterparties" ("**NFCs**") – all undertakings established in the EU other than financial counterparties and central counterparties; and
  - "third country entities" – all undertakings other than financial counterparties, non-financial counterparties and central counterparties.
- A further distinction is made among (i) FCs, between those whose OTC derivatives activity (including hedging activity) exceeds a specified level for certain asset classes and those whose OTC derivatives activity (including hedging activity) does not ("**Small FCs**"), and (ii) NFCs, between those whose OTC derivatives activity (excluding hedging activity) exceeds specified clearing thresholds ("**NFC+**") and those whose OTC derivatives activity (excluding hedging activity) does not ("**NFC-**").
- In respect of third country entities, certain EMIR obligations apply directly to such persons in specified circumstances. Other obligations may indirectly affect such persons where their counterparty to a derivative contract is an EU-established entity that is itself directly subject to those obligations. The application of such obligations to a given third country entity depends, among other things, on how that entity would be classified if it were established in the EU (i.e. whether it would be an FC, an NFC+ or an NFC-).
- In respect of entities established in Iceland, Liechtenstein and Norway, certain EMIR obligations may apply directly. This depends, however, on the status of incorporation of EMIR and related legislation into the EEA Agreement. Entities established in these jurisdictions should satisfy themselves as to their status under EMIR and complete the Master Regulatory Disclosure Letter accordingly.

#### Clearing Categorisation

As indicated in the "General Introduction" section above, the application of the clearing obligation – both in terms of whether the clearing obligation applies and, if so, the timeframe for implementation – depends on, among other things, how both entities to an OTC Derivative Contract are classified according to the taxonomy used in EMIR and related regulatory technical standards.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

- Certain entity types are not subject to the clearing obligation under EMIR. In general terms, these include (among other entities) NFC-s, non-undertakings, certain central banks, public authorities, multilateral development banks, other supranational bodies and, in certain circumstances, pension scheme arrangements.
    - For entity types that are subject to the clearing obligation (FCs (which are not Small FCs) and NFC+s), the regulatory technical standards which set out the detail of the application of the EMIR clearing obligation to interest rate and credit product OTC Derivative Contracts distinguish between category 1 entities, category 2 entities, category 3 entities and category 4 entities.

In respect of third country entities, the clearing obligation may apply (directly or indirectly) to a third country entity depending on, among other things: (a) the classification of its counterparty; and (b) how the third country entity would be classified if it were established in the EU.

**Exchange of Margin Requirements**

As indicated in the "General Introduction" section above, the obligation under EMIR to exchange margin in respect of uncleared OTC Derivative Contracts depends on, among other things, how both entities to an OTC Derivative Contract are classified according to the taxonomy used in EMIR.

- Certain entity types are not subject to the obligation to exchange margin under EMIR. In general terms, these include (among other entities) NFC-s, non-undertakings, certain central banks, public authorities, multilateral development banks and other supranational bodies.
- For entity types that are subject to the obligation to exchange margin (FCs and NFC+s), the regulatory technical standards distinguish between variation margin and initial margin ("**IM**"). The obligation to exchange IM is being phased in over a number of years by reference to the volume of trading conducted by a counterparty and its related group. The relevant threshold will continue to decrease annually until September 2020 (EUR 8 billion threshold).
- The European Supervisory Authorities have indicated that margin requirements should only apply in respect of physically-settled foreign exchange ("**FX**") forward contracts where both counterparties are "institutions" under Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013 (or are an equivalent entity located in a third country that would meet the definition of "institution" if located in the EU). As of 7 June 2019, European legislative efforts remain in draft form, however, there is also now an expectation that this treatment will be extended to physically-settled FX swaps.
- In respect of third country entities, the obligation to exchange margin may apply (directly or indirectly) to a third country entity depending on, among other things: (a) the classification of its counterparty; (b) how the third country entity would be classified if it were established in the EU; and (c) the third country entity's AANA.

## WHO SHOULD/SHOULD NOT COMPLETE THESE QUESTIONS?

These questions should not be completed by:

- central counterparties;
- trade repositories;
- trading venues.

All other undertakings that enter into derivatives **should** complete these questions, including those that are not established in the EU.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

Natural or legal persons who/which are not “undertakings” for the purposes of EMIR – “non-undertakings” – and who/which therefore consider themselves to be outside the scope of EMIR should answer the “Third Country Entity” question, answer “Yes” to the “Are you an entity that is fully or partially out of scope for EMIR?” question and then indicate that they are a non-undertaking.

In addition to the terms defined in Part II (*Definitions*) of Appendix A (*European Union*), please note:

- A trade repository is defined in Article 2(2) of EMIR as: “A legal person that centrally collects and maintains the records of derivatives”.
- A trading venue is defined in Article 2(4) of EMIR as: “A system operated by an investment firm or a market operator within the meaning of Article 4(1)(1) and 4(1)(13) of Directive 2004/39/EC (MiFID) other than a systematic internaliser within the meaning of Article 4(1)(7) thereof, which brings together buying or selling interests in financial instruments in the system, in a way that results in a contract in accordance with Title II or III of that Directive”. Note that the relevant references in EMIR to Directive 2004/39/EC of the European Parliament and of the Council dated 21 April 2004 (now repealed) have not been amended by the EMIR REFIT Regulation but should be read as references to Articles 4(1)(1), 4(1)(18) and 4(1)(20) (respectively) of Directive 2014/65/EU of the European Parliament and of the Council dated 15 May 2014 as indicated in Annex IV of that legislation.
- Neither “undertaking” nor “non-undertaking” is defined in EMIR. Please refer to the accompanying guidance for Question 2(b) on undertakings and non-undertakings for the European Commission’s (the “**EC**”) position on how a person should assess whether it is an “undertaking” for the purposes of EMIR.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

## QUESTION SPECIFIC GUIDANCE

### GENERAL

The statements provided in Appendix A (*European Union*) assume that the EMIR REFIT Regulation has come into effect. If Appendix A (*European Union*) is delivered to a Recipient prior to 17 June 2019, then for the period prior to 17 June 2019 such statements shall relate to the Named Entity's reasonable expectation of its status under the relevant provisions as of 17 June 2019.

### A. TRANSITIONAL PROVISIONS

**1. "*ISDA EMIR Classification Letter published by ISDA on 13 July 2015 and updated and further published on 13 April 2016 (the "EMIR Classification Letter")*"**

This statement is intended to clarify the relationship between the Master Regulatory Disclosure Letter and the EMIR Classification Letter. Pursuant to this provision, the statements made by the Named Entity in Appendix A (*European Union*) of the Master Regulatory Disclosure Letter will supersede all those statements made (if any) in the EMIR Classification Letter with the exception of the statements made by it by way of its responses to Questions 1, 2 and 3 of Appendix I (*EMIR Clearing Classification*), which shall continue to be effective.

The Master Regulatory Disclosure Letter does not include statements as to the Named Entity's clearing category under the various EMIR regulatory technical standards. This is because the staged implementation of the EMIR clearing obligation will no longer be relevant once the final phase-in of the clearing obligation under the existing regulatory technical standards occurs later in 2019. Instead, the drafting of Appendix A (*European Union*) preserves the validity of any existing statements relating to clearing categorisation exchanged between the parties under the EMIR Classification Letter.

Entities will find specific guidance as to how to answer each of Questions 1, 2 and 3 in the ISDA published *Explanatory memorandum to the form of the ISDA EMIR Classification Letter*.

**2. "*ISDA Regulatory Margin Self-Disclosure Letter published by ISDA on 30 June 2016 (the "Self-Disclosure Letter")*"**

The form of a number of the statements provided in Appendix A (*European Union*) are taken from Section 3 (*EU Information*) of the Self-Disclosure Letter. This statement is intended to clarify the relationship between the Master Regulatory Disclosure Letter and the Self-Disclosure Letter. Pursuant to this provision, the statements made by the Named Entity in Appendix A (*European Union*) will supersede those made by it in Section 3 (*EU Information*) of the Self-Disclosure Letter, which include sections on EU entity status, Third Country Entity status, EU branches, DSF Guarantees and EU AANA information.

**3. "*ISDA 2013 EMIR NFC Representation Protocol published by ISDA on 8 March 2013 (the "NFC Protocol")*"**

If the Named Entity elects to apply this provision, the Master Regulatory Disclosure Letter shall constitute a "Non-representation Notice" for the purposes of the NFC Protocol, such that subparagraph (i)(1) and, where not already disapplied, subparagraph (i)(2) of the NFC Representation is disapplied and does not form part of the NFC Representation (each as defined in the NFC Protocol).

If the Named Entity does not elect to apply this provision and it has adhered to the NFC Protocol or otherwise incorporates the Attachment to the NFC Protocol, the statements made by it pursuant to any such adherence or incorporation (as applicable) will remain unaffected by the Master Regulatory Disclosure Letter. In such circumstances, the Named Entity should consult its legal advisers as to the continuing accuracy and impact of such statements.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

## B. REGULATORY DISCLOSURE STATEMENTS

Guidance is included in the Master Regulatory Disclosure Letter itself in respect of entities in the European Economic Area countries of Iceland, Liechtenstein and Norway. The procedure for incorporating European legislation into the EEA Agreement is complex and entities established in these countries should consult their legal advisers if they are unsure of their status under EMIR after the EMIR REFIT Regulation enters into force on 17 June 2019.

The guidance also indicates that the Named Entity should seek to answer every question in the Master Regulatory Disclosure Letter if it is established in the EU. If the Named Entity is a third country entity, it should answer all questions except Question 4(c) and Question 4(d), which relate to Pension Scheme Arrangements, and it should do so on the basis of its categorisation *were* it established in the EU.

Certain EMIR obligations apply both to contracts between entities established in the EU and contracts where one counterparty (or both counterparties in certain circumstances) is established in a third country but would be subject to the relevant obligation were it established in the EU. A non-EU entity's *equivalent* categorisation is, therefore, an important data point for its counterparty to receive.

**Question 1(a) "Third Country Entity"**

The term "third country entity" is not defined in EMIR. However, in the context of the application of certain obligations, EMIR distinguishes between entities that are established in the EU and entities that are not established in the EU. For the purposes of Question 1(a) therefore, a "third country entity" means an entity that is not established in the EU (subject to the points below).

The meaning of "established" has also not been defined in this context – existing commentary from European authorities suggests that it refers to the jurisdiction in which an entity is incorporated or otherwise constituted (rather than any physical presence from which it does business, to the extent that this differs from its jurisdiction of incorporation or constitution); for example, an entity which is incorporated outside the EU but has a physical presence in the EU by way of a branch would still be a third country entity. *Each entity must determine for itself where it is "established" for these purposes.*

It is important to note that Question 1(a) should be answered subject to the following:

- it should still be answered by an entity which is wholly or partially exempt from EMIR (which is addressed in subsequent questions); and
- an entity which would be a "third country entity" on the basis of its establishment alone should still answer that it is not a third country entity if that entity is in fact a "financial counterparty" under EMIR. This is of particular relevance to a non-EU alternative investment funds ("**AIFs**") managed by a manager authorised or recognised in accordance with the Alternative Investment Fund Managers Directive (Directive 2011/61/EU of the European Parliament and of the Council dated 8 June 2011, or the "**AIFMD**"), which would be a "third country entity" on an establishment-only test but is a financial counterparty for EMIR purposes.

*Where an entity elects here that it is a "Third Country Entity", the remainder of the elections made by the entity should be read in that context.*

*Natural or legal persons who/which are not "undertakings" for the purposes of EMIR – "non-undertakings" – and who/which therefore consider themselves to be outside the scope of EMIR should answer Question 1(a).*


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

**Question 1(b) "EU branches"**

Third country entities may be directly subject to obligations under EMIR in limited scenarios. These include circumstances in which a relevant contract between two third country entities is considered as having a direct, substantial and foreseeable effect within the EU. Article 2(2) of Commission Delegated Regulation (EU) No 285/2014 dated 13 February 2014 provides that a contract will be considered as having a direct, substantial and foreseeable effect within the EU where both third country entities enter into the contract through branches in the EU and would qualify as FCs if they were established in the EU.

Entities should carefully consider whether they are acting through a branch in the EU and consult with their legal advisers as to the relevant factors which should be considered in making this determination.

***The Named Entity's response to this question may not be uniform across all of its trading relationships and may depend on the identity of the relevant Recipient.***

**Question 1(c) "DSF Guarantee(s)"**

Third country entities may be directly subject to obligations under EMIR in limited scenarios. These include circumstances in which a relevant contract between two third country entities is determined to have a direct, substantial and foreseeable effect within the EU. Article 2(1) of Commission Delegated Regulation (EU) No 285/2014 dated 13 February 2014 provides that a contract shall be considered as having a direct, substantial and foreseeable effect within the EU when at least one of the third country entities benefits from a guarantee provided by an FC established in the EU which covers all or part of its liability resulting from that contract and that guarantee meets two additional conditions set out in Article 2(1).

The conditions that are required to be met are technical and entities should consult with their legal advisers if they have any related questions before they make a determination for the purposes of Question 1(c).

***The Named Entity's response to this question may not be uniform across all of its trading relationships and may depend on the identity of the relevant Recipient.***

**Question 2(a) "Fully or partially out of scope for EMIR"**

Question 2(a) intends to identify those entities which are expressly exempt from EMIR, either in whole or in part, and those natural or legal persons who consider themselves to be outside the scope of EMIR by reason of not being an "undertaking" for the purposes of EMIR ("non-undertakings").

***Exempt entities***

Certain specified types of entity are wholly exempt from the EMIR obligations; certain other specified types of entity are exempt in part.

An entity will be wholly exempt – i.e. none of the EMIR obligations will apply to it – if it falls within one of the types of entity listed in Article 1(4) of EMIR. An entity will be partially exempt – i.e. none of the EMIR obligations will apply to it *other than the reporting obligations* – if it falls within one of the types of entity listed in Article 1(5) of EMIR.

Subject to the next paragraph, the lists of wholly and partially exempt entities are static – in this context there is no concept of "equivalence" for entities that: (a) are not specifically named; or (b) in the case of a defined group of exempt entities, do not fall within that definition.

The EC has the power to extend the list of entities that are wholly exempt from EMIR (but not the list of entities that are partially exempt). It may therefore be the case that an entity not currently exempt from EMIR could become exempt in future, *at which point it should amend its response to Question 2(a)*.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

*Each entity must determine for itself whether it falls within one of the types of entity listed as being wholly or partially exempt.*

These exemptions are distinct from the time-limited exemption from clearing for certain types of OTC derivative entered into by Pension Scheme Arrangements ("**PSAs**").

***Non-undertakings***

Natural or legal persons who/which are not "undertakings" for the purposes of EMIR – "non-undertakings" – and who/which therefore consider themselves to be outside the scope of EMIR should answer "Yes" to Question 2(a) "Are you an entity that is fully or partially out of scope for EMIR?" and then indicate that they are a non-undertaking in Question 2(b).

Please refer to the accompanying guidance for Question 2(b) on undertakings and non-undertakings for the EC's position on how a person should assess whether it is an "undertaking" for the purposes of EMIR.

*Each natural or legal person must determine for itself whether it is or is not an undertaking for the purposes of EMIR.*

*If the Named Entity is fully or partially out of scope of EMIR, then it should only answer Question 2(a) and Question 2(b) and should not complete the remaining sections of Appendix A (European Union).*

**Question 2(b) "Select the entity type that is fully or partially out of scope"**

Each entity which has indicated that it falls outside the scope of EMIR by selecting "Yes" in response to Question 2(a) must specify the basis for that indication to confirm its entity type. These exemptions are distinct from the time-limited exemption from clearing for certain types of OTC derivative entered into by PSAs. If a PSA answers "No" to Question 2(a), such PSA should not answer Question 2(b).

The entity types are as defined in Part II (*Definitions*) of Appendix A (*European Union*). In addition, for ease of reference:

(i) in respect of the definition of an Article 1(4)(c) Entity, Article 1(4)(c) of EMIR was added by delegated act in accordance with Article 1(6) of EMIR, which required the EC to prepare a report assessing the international treatment of public bodies charged with or intervening in the management of the public debt and central banks (the report is available at https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A52013DC0158) and empowered the EC to adopt delegated acts (in accordance with Article 82 of EMIR) to amend the list set out in Article 1(4);

(ii) in respect of the definition of an Article 1(5)(a) Entity, the multilateral development banks listed under Article 117 of Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013 (this regulation repealed Directive 2006/48/EC of the European Parliament and of the Council dated 14 June 2006, to which Article 1(5)(a) of EMIR refers) are:

- the International Bank for Reconstruction and Development;
- the International Finance Corporation;
- the Inter-American Development Bank;
- the Asian Development Bank;
- the African Development Bank;
- the Council of Europe Development Bank;


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

- the Nordic Investment Bank;
- the Caribbean Development Bank;
- the European Bank for Reconstruction and Development;
- the European Investment Bank;
- the European Investment Fund;
- the Multilateral Investment Guarantee Agency;
- the International Finance Facility for Immunisation; and
- the Islamic Development Bank; and

(iii) in respect of the definition of Article 1(5)(b) Entity, "public sector entities" means non-commercial administrative bodies responsible to central governments, regional governments or local authorities, or to authorities that exercise the same responsibilities as regional governments and local authorities, or non-commercial undertakings owned by or set up and sponsored by central governments, regional governments or local authorities, and that have explicit guarantee arrangements, and may include self-administered bodies governed by law that are under public supervision.

*Each entity must determine for itself to which category it belongs.*

***A non-undertaking***

The concept of an "undertaking" is not defined in EMIR. The EC, in its EMIR FAQs, has given its interpretation of what constitutes an "undertaking" for EMIR purposes. In this regard, the EC notes the following:

- Undertaking could mean an "entity operating in one or more economic sectors".
- The qualification of an entity as an "undertaking" for EMIR purposes would also appear to depend on the nature of the activities carried out by that entity, rather than on the nature of the entity itself.
- The Court of Justice has also consistently held that, in the context of competition law, the concept of an undertaking covers any entity engaged in an economic activity, regardless of the legal status of the entity or the way in which it is financed. Therefore, the qualification of a specific entity as an undertaking depends entirely on the nature of its activities. As regards the concept of "economic activity", the Court has considered that any activity consisting in offering goods and services on a market is an economic activity, regardless of the entity's legal status and the way in which it is financed.
- Non-profit entities are also considered "undertakings" if they offer goods and services in the market.
- Individuals carrying out an economic activity are also considered to be undertakings, provided they offer goods and services in the market.

The EC also notes, however, that the exercise of public authority or powers would not be considered an economic activity. In this respect, where authorities emanating from the relevant State act in their capacity as public authorities, they would not be considered undertakings.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

Accordingly, the EC asserts that the term “undertaking” is determined by reference to activities instead of entities and that, against this background, the term “undertaking” would include entities, regardless of their legal status, performing economic activities in the market.

*If the Named Entity has checked “Yes” in response to Question 2(a), it should answer Question 2(b).*

*If the Named Entity is fully or partially out of scope of EMIR, then it should answer Question 2(a) and Question 2(b) and should not complete the other sections of Appendix A (European Union).*

**Question 3 “EMIR entity type”**

“FC” and “NFC” are as defined in Part II (*Definitions*) of Appendix A (*European Union*).

Entities should note that the EMIR REFIT Regulation expands the scope of the definition of “financial counterparty” in Article 2(8) of EMIR.

Pursuant to the EMIR REFIT Regulation, central securities depositaries authorised in accordance with Regulation (EU) No 909/2014 of the European Parliament and of the Council dated 23 July 2014 are now in scope of EMIR’s FC definition, and the inclusion of undertakings for collective investment in transferable securities (“**UCITS**”) in the definition will be limited to those UCITS that are not set up exclusively for the purpose of serving one or more employee share purchase plans.

The scope of the definition of FC is also amended in respect of AIFs. Entities can obtain more detailed guidance as to the changes to this category of entity in the ISDA published *EMIR REFIT: Application to alternative investment funds (AIFs)*.

**Question 4(a) “Small FC”**

Question 4(a) is intended to help entities and their counterparties determine whether the EMIR clearing obligation applies to their OTC Derivative Contracts.

“Small FC” is defined in Part II (*Definitions*) of Appendix A (*European Union*). Pursuant to the EMIR REFIT Regulation, only certain FCs will remain subject to the clearing obligation under the revised form of Article 4 of EMIR. Article 4a(1) of EMIR provides that an FC that (i) does not calculate its positions for the purposes of that Article, or (ii) does calculate its positions but where the result of that calculation exceeds any of the clearing thresholds specified pursuant to point (b) of Article 10(4) of EMIR, shall establish clearing arrangements within four months after the related notification to the European Securities and Markets Authority (“**ESMA**”) and the relevant competent authority. The term “Small FC” refers to the category of FCs that do not meet the requisite criteria set out in Article 4a(1) and, subject to the detailed provisions of that Article, are not subject to the clearing obligation.

Entities should note that Small FCs will nevertheless be subject to the risk mitigation obligations in Article 11 of EMIR.

The Named Entity may prefer to select “Decline to answer” for a number of reasons. For example, the Named Entity may have chosen not to perform the relevant calculations required by Article 4a(1) or may not yet have finalised such calculations. In such circumstances, the Named Entity may prefer not to positively indicate that they are *not* a Small FC.

*If the Named Entity has checked (i) “FC” in response to Question 3, it should answer Question 4(a), or (ii) “NFC” in response to Question 3, it should not answer Question 4(a) or any other question in Section 4 and should continue to Section 5.*


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

**<u>Question 4(b) “FC clearing start date”</u>**

Question 4(b) is intended to indicate whether an FC benefits from a four month grace period before they are obliged to clear and, if so, the expiry date of any such grace period.

Article 4a(1) of EMIR provides that an FC that (i) does not calculate its positions for the purposes of that Article, or (ii) does calculate its positions but where the result of that calculation exceeds <u>any of the clearing thresholds</u> specified pursuant to point (b) of Article 10(4) of EMIR, shall establish clearing arrangements within four months after the related notification to ESMA and the relevant competent authority.

To the extent that an FC *is already* subject to the clearing obligation at 17 June 2019, Article 4(a)(2) of EMIR provides that such an FC should continue to comply with its clearing obligations unless and until it demonstrates to the relevant competent authority that it no longer exceeds the clearing threshold. In such circumstances, the Named Entity should select “The four month period has expired or is otherwise not applicable”.

*If the Named Entity has checked (i) “No” or “Decline to answer” in response to Question 4(a), it should answer Question 4(b), or (ii) “NFC” in response to Question 3, it should not answer Question 4(b) or any other question in Section 4 and should continue to Section 5.*

**<u>Question 4(c) “Type of Pension Scheme Arrangement”</u>**

“Pension Scheme Arrangement” is as defined in Part II (*Definitions*) of Appendix A (*European Union*).

The options shown in Question 4(c) correspond with the definition of Pension Scheme Arrangement in Article 2(10) of EMIR and are as defined in Part II (*Definitions*) of Appendix A (*European Union*).

*If the Named Entity (i) has checked “is not a Third Country Entity” in response to Question 1(a) and (ii) is a Pension Scheme Arrangement, it should answer Question 4(c).*

**<u>Question 4(d) “Use of the Pension Scheme Arrangement Exemption”</u>**

The Pension Scheme Arrangement Exemption (“**PSA Exemption**”) is set out in Article 89 of EMIR and exempts certain PSAs, and certain entities related to PSAs, from having to clear contracts which meet set criteria. As of 7 June 2019, the temporary exemption under Article 89 is scheduled to expire on 18 June 2021. However, that timing may be further extended pursuant to the discretion set out in Article 85 of EMIR.

Question 4(d) is intended to help PSAs inform their counterparties as to whether the PSA Exemption should be treated as applicable in respect of some or all trades entered into by such PSA on an on-going basis. The aim is to remove, where possible, the need for the PSA to confirm the application of the PSA Exemption with each counterparty each time it enters into an uncleared trade. The statements made by the PSA are (only) in respect of trades to which the Recipient is party.

The first option, “All Contracts”, is broad, covering both trades which would otherwise have to be cleared and also trades which are, in any event, not subject to mandatory clearing. This is intended to allow the PSA:

(i) to say (essentially) that the exemption applies to all trades the PSA enters into which, but for the exemption, would have to be cleared (so the PSA is not required to clear any trades but might choose to clear trades on a voluntary basis); and

(ii) to give the parties it faces comfort relating to Articles 382(4)(c) and 482 of the Capital Requirements Regulation (Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013) with respect to credit valuation adjustment risk.

The second option, “All Contracts To Which Mandatory Clearing Would Otherwise Apply”, is narrower than the first, applying only to trades which would otherwise have to be cleared. It says (essentially) that the


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

exemption applies to all trades the PSA enters into which, but for the exemption, would have to be cleared (so the PSA is not required to clear any trades but might choose to clear trades on a voluntary basis).

The third option, "No General Statement Made", is intended to allow the PSA to say (essentially) that:

(i) while it is not making a general statement as to whether or not the PSA Exemption applies to all contracts (so the PSA may or may not be required to clear trades);

(ii) if it does request to enter a trade on an uncleared basis where such trade would, but for the exemption, be subject to mandatory clearing, then it is requesting to trade uncleared because the PSA Exemption applies.

*If the Named Entity (i) has checked "is not a Third Country Entity" in response to Question 1(a) and (ii) is a Pension Scheme Arrangement or an entity established to provide compensation to members of a Pension Scheme Arrangement in case of default, it should answer Question 4(d).*

**Question 4(e) "Institution"**

In Question 4(e), the Named Entity is asked to confirm whether it is an "institution" for the purposes of Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013.

The European Supervisory Authorities have indicated that margin requirements should only apply in respect of physically-settled foreign exchange ("**FX**") forward contracts where both counterparties are "institutions" under Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013 (or are an equivalent entity located in a third country that would meet the definition of "institution" if located in the EU).

An "institution" is a credit institution, as defined under Regulation (EU) No 575/2013 of the European Parliament and of the Council dated 26 June 2013, or an investment firm, as defined under Directive 2014/65/EU of the European Parliament and of the Council dated 15 May 2014.

*If the Named Entity has checked (i) "FC" in response to Question 3, it should answer Question 4(e), or (ii) "NFC" in response to Question 3, it should not answer Question 4(e) or any other question in Section 4 and should continue to Section 5.*

**Question 5(a) "Clearing threshold"**

"NFC+" and "NFC-" are as defined in Part II (*Definitions*) of Appendix A (*European Union*).

The application of the EMIR obligations to an NFC, both in terms of whether the obligations apply and, if so, the extent to which they apply, depends on, among other things, whether that NFC is classified as an NFC+ or an NFC-.

The methodology for distinguishing between these two categories of NFC is set out in Article 10 of EMIR and is based on a comparison of the aggregate month-end average positions of the entity for the previous 12 months, calculated at a group level and without regard to positions that are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity of the NFC or of that group, against clearing thresholds specified in Article 11 of Commission Delegated Regulation (EU) No 149/2013 dated 19 December 2012.

*If the Named Entity has checked (i) "NFC" in response to Question 3, it should answer Question 5(a), or (ii) "FC" in response to Question 3, it should not answer Question 5(a) or any other question in Section 5 and should continue to Section 6.*


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

**<u>Question 5(b) "OTC credit derivative contracts" and Question 5(d) "OTC interest rate derivative contracts"</u>**

In answering Question 5(b) and Question 5(d), the Named Entity provides the Recipient with further detail about the results of its calculations under Article 10(2) of EMIR, namely whether the Named Entity is above or below each clearing threshold in respect of the classes of OTC Derivative Contracts currently subject to mandatory clearing, being certain types of OTC credit derivative contracts and OTC interest rate derivative contracts.

This information is required because Article 10(2) of EMIR provides that, where an NFC+ calculates its positions in accordance with that provision, it will only become subject to the clearing obligation in respect of those asset classes for which the result of its calculation exceeds the related clearing threshold. This means that an NFC+ may not be required to clear one or more classes of derivative contract that would otherwise be subject to the clearing obligation.

The following classes of OTC Derivative Contract have been declared subject to the clearing obligation:

- certain interest rate derivative contracts denominated in the G4 currencies (EUR, GBP, USD and JPY) set out in the Annex to Commission Delegated Regulation (EU) 2015/2205 dated 6 August 2015, including fixed-to-floating interest rate swaps, basis swaps, forward rate agreements and overnight index swaps;
- certain credit default derivative contracts, the relevant classes of which are set out in the Annex to Commission Delegated Regulation (EU) 2016/592 dated 1 March 2016, namely untranched iTraxx Index credit default swaps (Europe Main, 5-year tenor, series 17 onwards, with EUR as settlement currency) and untranched iTraxx Index credit default swaps (Europe Crossover, 5-year tenor, series 17 onwards, with EUR as settlement currency); and
- certain interest rate derivative contracts denominated in some non-G4 currencies (SEK, PLN and NOK) set out in the Annex to Commission Delegated Regulation (EU) 2016/1178 dated 10 June 2016, including fixed-to-floating interest rate swaps and forward rate agreements.

The Named Entity may prefer to select "Decline to answer" in respect of one or both of these questions for a number of reasons. For example, the Named Entity may have chosen not to perform the relevant calculations required by Article 10 or may not yet have finalised such calculations. In such circumstances, the Named Entity may prefer not to positively indicate that they are *above or below* the relevant clearing threshold.

*If the Named Entity has checked (i) "NFC" in response to Question 3 and "NFC+" in response to Question 5(a), it should answer Question 5(b) and Question 5(d), or (ii) "FC" in response to Question 3, it should not answer Question 5(b) or Question 5(d) or any other question in Section 5 and should continue to Section 6.*

**<u>Question 5(c) "Clearing date for OTC credit derivative contracts" and Question 5(e) "Clearing date for OTC interest rate derivative contracts"</u>**

If an NFC+ has indicated that it exceeds the clearing threshold for one or more classes of derivative contract pursuant to Question 5(b) and Question 5(d), Question 5(c) and Question 5(e) are intended to indicate whether that entity currently benefits from a four month grace period in respect of such classes of derivative contract before they are obliged to clear relevant contracts and, if so, the expiry date of any such grace period.

Article 10(2) of EMIR provides that an NFC that (i) does not calculate its positions for the purposes of that Article, or (ii) does calculate its positions but where the result of that calculation exceeds one or more of the clearing thresholds specified pursuant to point (b) of Article 10(4) of EMIR, shall establish clearing arrangements <u>for the relevant classes of derivative contract</u> within four months after the related notification to ESMA and the relevant competent authority.


Copyright © 2019 by International Swaps and Derivatives Association, Inc.

To the extent that an NFC *is already* subject to the clearing obligation at 17 June 2019, Article 10(2) of EMIR provides that such NFC should continue to comply with its clearing obligations unless and until it demonstrates to the relevant competent authority that it no longer exceeds the clearing threshold. In such circumstances, the Named Entity should select "The four month period has expired or is otherwise not applicable".

*If the Named Entity has checked (i) "Yes" or "Decline to answer" in response to Question 5(b), it should answer Question 5(c), (ii) "Yes" or "Decline to answer" in response to Question 5(d), it should answer Question 5(e), or (iii) "FC" in response to Question 3, it should not answer Question 5(c) or Question 5(e) or any other question in Section 5 and should continue to Section 6.*

**Questions 6(a), 6(b) and 6(c) "AANA information"**

Article 11(3) of EMIR provides that FCs and NFC+s must implement risk-management procedures requiring the "timely, accurate and appropriately segregated exchange of collateral" in respect of certain uncleared OTC Derivative Contracts. These requirements apply irrespective of whether an FC is a "Small FC" or, in respect of an NFC+, if that entity has determined that it falls below the clearing threshold in respect of one or more classes of derivative contract.

Article 36 of Commission Delegation Regulation (EU) 2016/2251 dated 4 October 2016 (the "Margin RTS") provides that the obligation to exchange IM applies where *both counterparties* to an OTC Derivative Contract have, or are part of a group that has, an AANA above a certain monetary threshold.

Each entity's AANA is calculated in accordance with Article 39 of the Margin RTS as the average of the total gross notional amount of its uncleared OTC derivatives (aggregated with the uncleared derivatives of its group affiliates) recorded on the last business days of March, April and May of the relevant year. This calculation also includes all intra-group uncleared OTC Derivative Contracts. An entity's "group" includes its ultimate parent and each of that ultimate parent's subsidiaries, including affiliates located outside of the EU.

By answering Question 6(a) and Question 6(b), therefore, the Named Entity provides the Recipient with information required for an AANA calculation to be made for the purposes of the exchange of IM.

In Question 6(c), the Named Entity is asked to confirm whether it has already crossed an applicable AANA threshold or indicate which year (if any) it expects to cross a relevant threshold (i.e. either 1 September 2019 (EUR 750 billion notional amount threshold) or 1 September 2020 (EUR 8 billion threshold)).

*If the Named Entity has checked (i) "FC" in response to Question 3 or, (ii) "NFC" in response to Question 3 and "NFC+" in response to Question 5(a), it should answer Question 6(a), Question 6(b) (if the Named Entity has checked "Yes" in response to Question 6(a)) and Question 6(c).*


Copyright © 2019 by International Swaps and Derivatives Association, Inc.