ISDA response to ESMA consultation on the Draft technical standards to further detail the new EMIR clearing thresholds regime[1]

General Remarks:

We welcome the opportunity to provide comments to ESMA's consultation on draft regulatory technical standards (RTS) amending the RTS on the clearing thresholds (CT), further to EMIR 3 Article 4a(4) and 10(4)(b).

We have a number of comments on the level of granularity of data provided by ESMA in the consultation paper, on the methodology followed to define the levels of the CTs, and on the interaction with the active account requirements (AAR). We also suggest a proposal in relation to the implementation of the new regime which we believe is aligned with the simplification and burden reduction ambitions of the EU.

On ESMA's approach to defining the level of the new set of thresholds

We are concerned that the data provided by ESMA in the consultation paper does not allow to fully ascertain the impact of the revised set of thresholds. ESMA explains that the level of the clearing thresholds for uncleared positions has been defined to "capture a similar population of entities and notional, compared to the current scope of CTs" by looking at the impact on the population captured by aggregating financial counterparties (FCs) and non-financial counterparties (NFCs). However, at the same time, the set of aggregated CTs applying to FCs based on cleared and uncleared transactions remains the same for interest rate derivatives (IRDs) and credit derivatives.

The data provided by ESMA in the consultation paper does not allow to ascertain which set of the CTs – between the cleared and uncleared CTs – would be the test which brings the majority of FCs within the clearing obligation. Assuming the aggregate CT would be the test which brings the majority of FCs within the clearing obligation, attempting to capture the same number of entities and notional through the uncleared CT either means that the aggregate CT appears unnecessary, or is likely to overestimate the magnitude of the reduction of the CT which is necessary to capture the same population under the revised CTs. This means that there might be a non-negligible number of FCs that are currently under the CT, and that will continue to be so under the aggregate CT, but that will be brought above the CT based on uncleared transactions. In other words, it is not entirely evident from ESMA's analysis which of the aggregate CT or the uncleared CT first brings firms within the scope of the clearing obligation, and whether ESMA has taken this aspect into account when calculating the values for the uncleared CTs.

We also note that per EMIR 3 Recital 9 and Article 4a(4), the aggregate clearing threshold applying for FCs is to ensure a similarly prudent coverage for the clearing obligation, in light of the change in methodology, looking only at uncleared transactions for the CT. However, keeping the aggregate CT at the same level as the current threshold, which by definition, will capture the same population as currently, does not appear in line with the purpose defined under EMIR 3 for the aggregate CT, which is to serve as a backstop under the new methodology. As a result, if the uncleared threshold is indeed meant to capture a similar population, the backstop nature of the aggregate threshold suggests that they should be significantly higher than the current level.

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[1] ESMA74-1049116225-632 Consultation Paper on the Draft technical standards amending Regulation (EU) 149/2013 to further detail the new EMIR clearing thresholds regime

On the interplay with AAR

Because of the way in which Article 7a(1) refers to "the clearing threshold" as part of the definition of the scope of the active account requirement, any revision of the clearing threshold should come with an impact assessment on the population captured under the AAR. As a result of Article 7a(1), the clearing threshold methodology is not only an integral part of the definition of the scope of the clearing obligation, but also an integral part of the definition of the scope of the active account requirement. ESMA should therefore include an impact analysis of the proposed levels on the scope of the AAR.

Timing for implementation of the methodology in light of simplification and burden reduction

The revised methodology, by design, introduces changes in terms of how firms perform calculations. It may also lead to changes on the possible outcome of the calculation – with significant diverging impacts for FCs and NFCs in the process of the initial application period of the revised RTS. For FCs, the new methodology does imply monitoring two sets of thresholds ("uncleared" and "aggregate"), which introduces additional complexity and potentially brings some financial counterparties over the threshold while they are currently not subject the clearing obligation, as outlined in our response in more detail. For NFCs, the new methodology is less onerous, and generally easier to calculate than the current methodology, especially given that it is determined at entity rather than group level, which is in line with the EU simplification objective.

Because of this, we would encourage ESMA to seize the opportunity for burden reduction by adopting a tailored implementation approach, which would enable those firms wishing to reap the benefits of the new simplified methodology to do so as soon as they are ready to do so, while also providing an appropriate implementation period for those firms that will require more time to implement the new methodology.

For example, EU NFCs may benefit from a swift implementation of the new regime in light of futures traded in the UK counting towards the clearing threshold under the current methodology, as these are treated as OTC derivatives due to the absence of EU-UK trading venue equivalence post Brexit (even though the UK version of EMIR does not include futures traded on EU exchanges within its clearing threshold). These exchange-traded derivatives are cleared, so would be excluded under the revised methodology for NFCs. On the other hand, financial counterparties would need to implement the envisaged dual regime (uncleared and aggregate thresholds) while being expected (further to ESMA's Q&A on EMIR Implementation, OTC Q&A 4 and 13[2]) to obtain representations from their clients on their status. Therefore, we encourage policymakers to adopt a tailored approach to the implementation of the new clearing threshold regime. The associated burden reduction for firms would also contribute to the EU's broader simplification and competitiveness efforts.

In light of this, ESMA could provide a much welcome accommodation by clarifying the date from which the new methodology of the CT takes effect, providing the following flexibility for firms:

- NFCs wishing to use the new methodology as soon as possible should be allowed to do so at any time from the date on which the RTS enters into force (i.e. 20 days after publication of the RTS in the EU Official Journal) with a backstop date by which they must begin using it,

[2] ESMA70-1861941480-52 Q&As on EMIR implementation

i.e. effectively providing in the RTS an option for NFCs to implement the new methodology as soon as they are ready to do so;

- In parallel, and to reduce the burden arising from the transition to the new methodology for all other firms, set an application date in the RTS to allow for a seamless transition with the window used for the current calculations against the existing CTs. Firms currently look at positions for the past 12 months as of 17 June (per the EMIR Refit go-live date) every year. When finalising the RTS, ESMA should include an appropriate application date to ensure that the new methodology would take effect on the same date (except for those NFCs that choose to implement the new methodology earlier, i.e. as soon as they are ready to do so from the date on which the RTS has entered into force);

- In relation to ESMA's Q&As on EMIR Implementation, OTC Q&A 4 and 13, counterparties should not be expected to obtain new representations from their counterparties on their status as a result of the entry into force of the new RTS. For NFCs wishing to apply the new methodology within the timeframe referenced above, the onus would be on them to inform their counterparties that their EMIR classification status has changed.

We have provided in Appendix some suggested drafting to include in the draft RTS, under a revised Article 2, to provide for this accommodation.

Q1: Do you agree that the aggregate thresholds should only be set for those asset classes subject to the CO i.e. IRDs and credit derivatives? If not, please elaborate.

We agree that it is unnecessary to set aggregate thresholds for asset classes not subject to the CO.

On the proposal to set aggregate thresholds for IRDs and credit derivatives

As set out under EMIR 3 Recital 9, ESMA is empowered to "set an aggregate clearing threshold, if needed", the objective being defined "in order to ensure that the current prudent coverage of the clearing obligation is not affected by the new methodology". However, we note that the clearing thresholds set under the new methodology, i.e. based on uncleared transactions, have been set by ESMA with the intention to "capture a similar population of entities and notional, compared to the current scope of the CTs", as set out under paragraph 56 of the consultation paper. In particular, ESMA explains how the proposed levels of the CTs "would allow to capture a similar population of entities and notional" (paragraph 58), with €1.8 billion as the new CT achieving that objective for IRDs (paragraph 60), and €700 million as the new CT achieving that objective for credit derivatives (paragraph 61).

We understand this to mean that the proposed levels of the CTs for IRD and credit derivatives, based on the revised methodology, would ensure the same "prudent coverage" (Recital 9 of EMIR). Therefore, based on the objective set by EMIR 3 for the aggregate clearing thresholds, this would suggest that aggregate clearing thresholds are not necessary – because the same current coverage is achieved through the revised CT based on uncleared transactions, following ESMA's own analysis that led to the calibration of the uncleared CTs.

Given that adding a second set of thresholds adds complexity for firms, who will now have to compute positions against two sets of thresholds, the uncleared and aggregate thresholds, we recommend minimising the burden on firms by only setting an aggregate threshold where strictly necessary. We understand that one of the raison d'être of the aggregate clearing threshold, even if not explicitly noted in EMIR 3 text or recitals, is intended to ensure that counterparties do not fall out of the scope of the AAR, as suggested by ESMA under paragraph 52. With this in mind, an aggregate threshold only appears necessary for IRD products, given that credit derivatives are not part of the clearing services relevant to the AAR.

On the interplay with the AAR

We also draw ESMA's attention to Article 7a(1), which refers to counterparties "*that exceed the clearing threshold in any of the categories of derivative contracts referred to in paragraph 6 of this Article",* setting out the second cumulative condition ("condition 2") that must be met for counterparties to be subject to the AAR. In paragraph 27 of the consultation on the revised clearing thresholds, ESMA notes that stakeholders should refer to the ESMA CP on the AAR, without further assessing how the current revisions would affect the population captured under the AAR. However, through the scope of application of the AAR as set out under Article 7a(1), clearing thresholds – and whatever value needs to be used for the purposes of condition 2, which is a point that we discuss further – become an integral part of not just the scoping of clearing obligation, but also of the AAR. Because of this, any revision of the clearing thresholds, as consulted on as part of the current consultation paper, should consider, at least in a cost-benefit analysis, and ideally in the main impact analysis, how the revision of the CTs affects the population captured under the AAR.

Then, as regards the actual threshold to be used for the purposes of condition 2, we flag that if NFCs were to use the revised CT for OTC interest rate derivatives based on uncleared transactions for the purposes of condition 2, many NFCs may inadvertently become scoped in the AAR, while they would not have otherwise been subject to it absent a revision of the CT methodology, which led to a significant reduction of the IRD CT. We would suggest that ESMA clarifies that the aggregate CT on IRDs for FCs – the continuation of the current CT on IRDs of €3bn – be the value that NFCs also refer to when looking at condition 2 for the purposes of Article 7a(1), based on activity at the individual level (i.e. in accordance with the revised CT calculation methodology for NFCs which does not capture group activity), and also excluding hedging activity.

Q2: Do you agree with ESMA's proposal to maintain the aggregate thresholds at the current level i.e. 3 billion EUR for IRDs and 1 billion EUR for credit derivatives? If not, please elaborate.

The purpose of the aggregate thresholds, which is to serve as a backstop to ensure that a similar population is captured, suggests that they should be much higher than the current level.

ESMA's proposed approach consists in calibrating a new set of uncleared thresholds, as discussed in our response to Q1, to capture the same population as under the current CTs, in isolation from the aggregate thresholds. On top of this, the proposed aggregate threshold, which would remain at the current level, would also by default capture the same population in isolation from the uncleared threshold. This means that the new set of thresholds can logically only capture more entities. As such, this approach most likely does not meet the goal of capturing roughly the same number of entities, which is set out under Recital 9 of EMIR 3. We note that ESMA is empowered to set an aggregate threshold "if needed", to ensure the same prudent coverage. As a result, if the uncleared CTs do indeed capture a similar population, the backstop nature of the aggregate threshold suggests that they should be much higher than the proposed level.

Otherwise, the aggregate thresholds would not fulfil the purpose set in Recital 9 and Article 4a(4) of EMIR.

Q3: Do you agree with the proposed uncleared thresholds? If not, please elaborate, explain for which asset class(es) and, where possible, provide supporting data and elements.

We note that as a result of the revised methodology, looking at uncleared trades, ESMA has significantly lowered the value of the thresholds applicable to FCs and NFCs: the CT for credit and equity derivatives would be lowered by 30%, the CT for commodity derivatives by 25% and the CT for interest rate derivatives by 40%.

The significant reduction of the CTs in asset classes where clearing is not prevalent, such as for equity derivatives and commodity derivatives, may lead many FCs to become subject to the CO because of their uncleared activity in those classes, while under the current methodology, they would have remained under the clearing threshold. Because ESMA's calibration of the clearing thresholds for uncleared positions looks at the impact on the population captured by aggregating FCs and NFCs, the analysis might indeed show an unchanged population at the level of aggregation, obviating that more FCs might be subject to the CO under the new methodology than under the current approach.

We would welcome further economic justification for the revised level of the CTs. While we acknowledge that ESMA has sought to keep the population captured by the new set of CTs unchanged compared to current CTs, further information would be necessary to assess the appropriateness of the revised thresholds in light of the new methodology:

- ESMA does not provide data on the number of entities (breaking down between FCs and NFCs) and notional captured by the new CTs. Such data would be useful to understand the precise impact of the revised CTs. We note that in previous reports on the CTs, ESMA provided detailed data to assess the impact of changes to the CT levels (such as for example in Annex I of the Report on the review of the clearing thresholds under EMIR Refit, September 2022)[3]. In this consultation, ESMA does not provide the same level of granularity, hindering the understanding of the impact of the revised CTs;
- while ESMA explains that the great majority of notional in FX products is uncleared, such that it is intuitive that the CT would remain the same, for other categories, further economic justification underpinning the revised level of the threshold would be welcome. For example, ESMA proposes a substantial reduction of the CT level for equity derivatives and commodity derivatives. Further economic justification would be useful, especially as substantial volumes within those categories are not cleared. This would allow to better understand the impact of the revised CTs;
- the analysis on the impact of the uncleared CTs seems to be looking at the impact on the captured population in isolation from the separate aggregate CTs, which also results in capturing FCs based on their cleared and uncleared IRS and credit derivatives activity. The analysis provided by ESMA does not allow to understand which set of threshold would be binding; assuming that the aggregate CT would be the test which brings the majority of FCs within the clearing obligation, attempting to capture the same number of entities and notional through the uncleared CT either means that the aggregate CT appears unnecessary, or is likely

[3] ESMA70-451-502 Report on the Review of clearing threshold under EMIR

to overestimate the magnitude of the reduction in the CT necessary to capture the same population under the revised CTs.

We note that the reduction in the CT might have unintended consequences on the liquidity of commodity derivatives markets, as NFCs might have to self-limit their activity in those markets to avoid breaching the CT. The proposal for a €3bn threshold for commodity derivatives also does not account for the fact that commodity prices have increased since 2012, when the €3bn value was originally defined. It is also a substantial reduction from the €4bn value that was applicable since 2022.

In addition, many non-financial groups manage all their derivative trading activities through a single centralised legal entity, which faces the external market for non-centrally cleared OTC derivatives trading activity. This centralised trading entity may not draw any benefit from the amended requirements of EMIR 3 because there is no aggregation of NFC group activities in this scenario. As a result, the proposed amendment of the commodity derivatives CT to €3 billion (down from €4 billion) would represent a significant reduction in the amount of trading activity that a group with an EU-established centralised NFC trading entity could undertake without becoming an NFC+, with all the additional costs and burden that this would bring. This cliff edge effect is particularly problematic as going over the CT in the commodity derivative asset class brings all uncleared OTC derivatives of all asset classes into scope of uncleared margin requirements, even where these are for hedging purposes. The effect of this NFC+ classification is therefore magnified for those NFCs with large hedging requirements, which would put EU entities at a competitive disadvantage to non-financials from other jurisdictions, and could disincentivise hedging for those over the CT.

The report does not include evidence suggesting that a lower threshold is warranted under the new methodology for the CT. Given the objective of EMIR to mitigate systemic financial risk and the FSB's finding in its report on financial stability aspects of commodity markets[4], a reduced threshold may not contribute to addressing counterparty credit risk concerns, but instead exacerbate liquidity challenges of NFCs acting in commodity markets in the event of unexpected price spikes and associated margin demands.

Q4: Do you agree with ESMA's proposal not to introduce in the RTS separate thresholds for the various commodity derivatives sub-asset classes at this stage? If not, please elaborate.

We agree with ESMA's proposal not to introduce separate thresholds for the various commodity sub-asset classes in the RTS, and would recommend that ESMA does not do so in the future, in the spirit of simplicity and predictability of regulatory outcomes.

Q5: Do you agree with ESMA's proposal to have in the fifth bucket only commodity and emission allowance derivatives? Or do you consider that commodity derivatives should be singled out as a stand-alone category and another category for emission allowance derivatives introduced? Please elaborate.

We agree with ESMA's proposal to have in the fifth bucket only commodity and emission allowance derivatives. However, for the reasons set out above, we believe that this threshold should be higher than proposed.

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[4] The Financial Stability Aspects of Commodities Markets: The Financial Stability Aspects of Commodities Markets

We do not support a separate threshold for emission allowances as it would be operationally challenging and costly to implement.

Q6: Do you agree with ESMA's proposal not to introduce a sixth bucket for other derivatives at this stage? If not, please elaborate.

We agree with the proposal not to include a sixth bucket for other derivatives.

Q7: Do you agree with ESMA's proposal not to introduce more granular thresholds for commodity derivatives based on ESG factors at this stage? If not, please elaborate.

We agree.

Q8: Do you agree with ESMA's proposal not to introduce more granular thresholds for commodity derivatives based on crypto-related features at this stage? If not, please elaborate.

We agree.

Q9: Do you consider clarifications should be included in Article 10 of Commission Delegated Regulation (EU) No 149/2013? If yes, please specify and if possible, provide arguments and drafting suggestions.

We do not consider that further clarifications are necessary.

Q10: Do you consider other indicators should be monitored and assessed? If yes, please specify and if possible provide drafting suggestion.

We do not consider that other indicators should be monitored and assessed.

Appendix

We provide below some suggested drafting to accommodate our suggestion for an implementation date that would provide the option for NFCs to apply the new methodology as soon as they are ready to do so, while allowing other counterparties to apply the new methodology at a later date, appropriately calibrated to ensure a seamless transition from the existing methodology.

Article 2

Entry into force and application

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

It shall apply from 17 June 2026, except for counterparties referred to under Article 10(1) of Regulation (EU) No 648/2012, who may opt to apply it at any time before such date from the date of entry into force of this Regulation, and no later than 17 June 2026.

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