22 December 2022

Reform of the UK EMIR intragroup exemptions – ISDA Proposal

Background and overview

The UK EMIR[1] framework provides exemptions for intragroup transactions from the clearing and margin requirements that apply to OTC derivative transactions. These exemptions recognise that exempting intragroup transactions from clearing and margining requirements would enable counterparties to take advantage of the efficiency of intra-group risk management processes without increasing systemic risk.

However, the regime inherited from the EU makes it a condition of these exemptions for transactions between UK and non-UK group entities that there is an equivalence determination in place in respect of the relevant non-UK country. Although equivalence determinations are in place for some non-UK countries (including EEA Member States), there are many states for which no equivalence determination has yet been made or where the existing determination only applies to some categories of transactions. We also note that the European Commission EMIR 3 legislative proposal removes equivalence determination as a condition for exemptions for intragroup transactions from the clearing and margin requirements.

To mitigate the impact of this and as part of the 'onshoring' of EMIR at the end of the Brexit transitional period, the UK replaced the previous EU temporary derogation with a new UK Temporary Intragroup Exemption Regime (TIGER) from clearing and margin requirements.[2] TIGER continued the previously existing exemptions under the EU temporary derogation – and allowed counterparties to obtain new exemptions – for OTC derivative contracts between UK and non-UK group entities where no equivalence determination has been made in respect of the relevant non-UK country.

These temporary exemptions will continue to apply until 31 December 2023, unless an equivalence determination is made in respect of the relevant third country before then. HM Treasury can extend the duration of TIGER in certain circumstances.

In this paper, ISDA makes the following proposals:

1. That there should be permanent intragroup exemptions from margin and clearing requirements for OTC derivative contracts between UK and non-UK group companies that do not depend on the making of equivalence determinations in respect of non-UK countries.

[1] Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories as it forms part of UK law.

[2] Part 5 of the Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2019/335.

2. Other changes should be made to the intragroup exemptions, and the related exemptions from reporting and the derivatives trading obligation (DTO), to streamline the requirements inherited from the EU regime.
3. ISDA envisages that these changes would be implemented when UK EMIR is revoked and replaced by a new UK regime regulating OTC derivative transactions, as part of the UK future regulatory framework, using the powers under the Financial Services and Markets Bill. Since the replacement of UK EMIR is not expected to take effect until after end 2023 (see "Building a smarter financial services framework for the UK"), ISDA proposes that HM Treasury extends TIGER beyond that date to ensure that there is no disruption for firms in the interim period. ISDA requests that HM Treasury communicates its intention to extend TIGER beyond end 2023 at the earliest opportunity, ideally before the end of this year, and outlines its longer term intentions as soon as possible.
4. In the interim, ISDA also proposes that the FCA confirms that the UK DTO does not apply to transactions benefitting from TIGER.

1. New permanent exemptions from clearing and margin requirements for cross-border intragroup transactions

ISDA proposes that there should be permanent intragroup exemptions from margin and clearing requirements for OTC derivative contracts between UK and non-UK group companies, that do not depend on the making of equivalence determinations in respect of non-UK countries. This would enable firms who operate across jurisdictions to efficiently manage their business and would not steer assets/funding away from financing real economy activities to meet intragroup margining and clearing requirements.

The EU and the UK regimes have, in effect, operated on this basis since the introduction of clearing and margin requirements in 2016. The proposed new permanent exemption is thus a continuation of the existing regime. If new restrictions are to be introduced, there should be an evidence basis supporting the need for the new restrictions. We also note that the BCSB-IOSCO framework does not explicitly require intragroup initial margin (see p.21 FR03/2020 Margin requirements for non-centrally cleared derivatives).

In any event, there are other measures already in place to mitigate the risks of uncleared or unmargined intragroup transactions for UK banks and PRA-authorised investment firms via the restrictions on intragroup large exposures, 'Pillar 2' requirements, recovery and resolution planning and – for UK ring-fenced banks – additional ring-fencing rules regulating intragroup transactions. The UK regulators responsible for the prudential supervision of other major categories of counterparties subject to clearing and margin requirements also have firm-specific intervention powers that can be used to mitigate excessive risks should they materialise. In addition, the UK future regulatory framework will provide the UK regulators with sufficient flexibility to respond to any changing circumstances that suggest that new restrictions are appropriate.

2. Streamlining the exemptions from clearing and margin requirements and related provisions

ISDA also proposes other changes to the intragroup exemptions under UK EMIR, and the related exemptions from reporting under UK EMIR and the DTO under UK MiFIR,[3] to streamline the requirements inherited from the EU regime. See the proposals set out in Annex A.

ISDA considers that many of the other conditions that apply to these exemptions and that were inherited from the EU regime are overly complex, lack clarity and can be removed without an adverse impact on the regulatory outcomes intended to be achieved by the UK regime. In addition, there is an opportunity to simplify the processes for relying on these exemptions to reduce the burden on firms and the FCA.

3. Extending TIGER beyond end 2023

ISDA envisages that the changes proposed above would be implemented when UK EMIR is revoked and replaced by a new UK regime regulating OTC derivative transactions, as part of the UK future regulatory framework, using the powers under the Financial Services and Markets Bill. **Since the replacement of UK EMIR may not take effect until after end 2023, ISDA proposes that HM Treasury extends TIGER beyond that date to ensure that there is no disruption for firms in the interim period.**

HM Treasury could extend TIGER by using the existing power to extend the period of the exemption in respect of any third country in which a non-UK counterparty is established.[4] Alternatively, HM Treasury could use the powers under the Financial Services and Markets Bill to make transitional amendments to the existing regulations, pending their revocation under the Bill.[5]

Firms estimate that it would take them 12 months to prepare for expiry of the exemptions – currently due on 31 December 2023 – so it is crucial that they get an early indication from the UK authorities on their intentions. **ISDA requests that HM Treasury communicates its intention to extend TIGER beyond end 2023 at the earliest opportunity, ideally before the end of this year, and outlines its longer term intentions as soon as possible**

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3 Regulation (EU) No 600/2014 on markets in financial instruments as it forms part of UK law.

44 Under Regulation 84 of the Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2019/335.

5 Under clause 3 of the Bill.

4. Interim action in relation to the UK DTO

Since the adoption of EMIR Refit in 2018, the scope of the clearing obligation (CO) under EMIR and the DTO under MiFIR have not been aligned. To mitigate this, the FCA has been applying transitional relief to address the issue.

The Financial Services and Markets Bill will, when enacted, realign the scope of the DTO so that the DTO and the CO apply to the same classes of counterparties. [6]

However, the amendments in the Bill do not base the alignment between the DTO and the CO on transactions that are subject to the CO, as ISDA recommended in its response to the Wholesale Markets Review.

This is significant because the amendments do not address situations – at present or in the future – where certain transactions are exempted from the CO (on a temporary basis or otherwise) but do not (automatically) qualify for exemption from the DTO. This includes the exemption from the CO for intragroup transactions under TIGER, because – on a literal reading of MIFIR – those transactions do not appear to qualify for the exemption from the DTO for intragroup transactions (which is linked to the existence of an equivalence determination under Article 13 EMIR).

Similar issues arise in the EU with respect to the relationship between the EU DTO and the EU temporary derogation for intragroup transactions with third country affiliates, but it has always been understood by the market that the EU DTO does not apply to transactions benefitting from the derogation. Nevertheless, successive drafts of the amended MIFIR text under discussion among the EU Member States indicate that the EU will eliminate any remaining uncertainty in this regard by clarifying that any transaction that is not subject to the clearing obligation will not be subject to the derivatives trading obligation.

This issue would cease to arise under our proposals set out in the Annex as the permanent intragroup exemptions would apply to both the clearing and margin requirements and the DTO and would not be linked to the existence of an equivalence determination. **However, ISDA proposes that, as an interim measure, the FCA confirms that the UK DTO does not apply to transactions benefitting from TIGER.** This would confirm that the position under the UK DTO is aligned with the market understanding that the UK DTO does not apply to transactions benefitting from TIGER. The confirmation could take the form of a public statement or an e-mail that ISDA could share with its members.

Alternatively, HM Treasury could use its powers under the Financial Services and Markets Bill to make transitional amendments to UK MiFIR to clarify the position.

If you have any questions in relation to this paper, please contact Toby Coaker, Assistant Director, UK Public Policy, ISDA (TCoaker@isda.org).

[6] Paragraphs 15 and 16 of Schedule 2 to the Bill.

About ISDA

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 1,000 member institutions from 78 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter, LinkedIn, Facebook and YouTube.

Annex A

Future Regulatory Framework Review - UK EMIR

Intragroup exemptions - proposed reforms

The following tables make proposals for reforms of the current intragroup exemptions from clearing and margin requirements under UK EMIR and of the related exemptions from the reporting obligation under UK EMIR, the derivatives trading obligation under UK MiFIR and the own funds requirement for credit valuation adjustment risk under UK CRR.

Intragroup exemptions from clearing and margin requirements

UK EMIR	Subject matter	Current position	Proposal	Comments
Article 3	Definition of intragroup transaction	• Counterparties can only rely on the exemptions for transactions with non-UK group companies[7] if an equivalence decision is in effect for non-UK jurisdiction, subject to the temporary intragroup exemption regime under SI 2019/335, which expires at end 2023 (although HM Treasury can extend the regime in some circumstances). • FCs can only rely on the exemptions for transactions with group companies if the other group company is (a) a financial counterparty, a financial holding	• An OTC derivative is an intragroup transaction if both counterparties are members of the same group. • The additional conditions do not apply.	• The proposal would simplify what is an overly complex definition. • The proposal would eliminate conditions which add little regulatory value, in particular the requirement for an equivalence assessment of non-UK jurisdictions. • The proposal would not give rise to additional compliance costs for firms as the definition of intragroup transaction

[7] The drafting of Article 3 is difficult to follow as in some cases it refers to FCs and NFCs when it is intended to refer to counterparties that are not established in the EU and refers to "the financial counterparty" when it is intended to refer to the other counterparty to the transaction with the FC.

UK EMIR	Subject matter	Current position	Proposal	Comments
		company, a financial institution or an ancillary services undertaking subject to appropriate prudential requirements or (b) a non-financial counterparty. • Counterparties can only rely on the exemptions for transactions with group companies if they are both subject to the same consolidation on a full basis (based on a complex definition, which - for groups headed by a non-UK parent - partly relies on the equivalence of the relevant accounting standards used by the group). • Counterparties can only rely on the exemptions where both counterparties are subject to an appropriate centralised risk evaluation, measurement and control procedures (but there is no clear definition of what procedures are regarded as appropriate). • Counterparties are part of the same group if they are linked by a parent-subsidiary relationship or are subsidiaries of a common parent (as defined in the Companies Act) or are		would be broader (not narrower). • There would also be no need to "grandfather" existing exemptions. Note: Consider aligning the definition of "group" with the FSMA definition of "immediate group" (which would exclude counterparties linked by a "common management relationship") or "group" (which would include undertakings in which a group member holds a "participating interest").

UK EMIR	Subject matter	Current position	Proposal	Comments
		linked by a "common management relationship" (as defined in UK CRR).		
Article 4(2)	Exemption from clearing obligation for intragroup transactions	• The exemption automatically applies to intragroup transactions between two UK counterparties if both counterparties have notified FCA and a 30-day waiting period has expired without the FCA objecting. • The exemption applies to intragroup transactions between a UK and a non-UK counterparty if the UK counterparty notifies FCA and the FCA has approved the use of the exemption within 30 days. • No exemption is available for transactions between two non-UK counterparties which are part of the same group (where the clearing obligation applies to them on the basis that the transaction has a direct, substantial and foreseeable effect in the UK).	• The exemption automatically applies to transactions between members of the same group. • The additional conditions do not apply. • The clearing obligation does not apply to transactions between two non-UK counterparties (or, if it is to apply to transactions between two UK branches of non-UK FCs, those branches are allowed to rely on the exemption on the same terms as UK counterparties).	• The proposal would simplify and clarify the process for firms. • PRA and FCA can rely on their existing powers and the new power proposed below to obtain information about the use of the exemption.[8] • The proposal would end the extraterritorial application of the UK clearing obligation to transactions between non-UK counterparties (which adds little regulatory value).

[8] For non-authorised counterparties, see the FCA's existing powers under regulation 7 of the Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) Regulations 2013/504 to require information to determine whether they have complied with UK EMIR.

UK EMIR	Subject matter	Current position	Proposal	Comments
		• The provisions do not explicitly state the basis on which the FCA can object or refuse approval. • There is no explicit procedure allowing the FCA to shorten the waiting period by approving the use of the exemption. • There is no procedure for counterparties to challenge an adverse decision by FCA (other than judicial review).		
Article 11(5), (8) and (9)	Exemption from margin requirements for intragroup transactions	• The exemption automatically applies to intragroup transactions between two UK counterparties if the first additional condition below is satisfied. • The exemption applies to intragroup transactions between a UK FC and a non-UK counterparty if the UK FC obtains the FCA's prior approval (which may be granted partially or fully) and if both additional conditions below are satisfied (but there is no explicit statement of the	• The exemption automatically applies to transactions between members of the same group. • The additional conditions do not apply. • The margin obligation does not apply to transactions between two non-UK counterparties (or, if it is to apply to transactions between two UK branches of non-UK FCs, those branches are allowed to rely on the	• The proposal would simplify and clarify the process for firms in relation to transactions with non-UK group companies. • PRA and FCA can rely on their existing powers and the new power proposed below to obtain information about the use of the exemption.[9] • The proposal would eliminate conditions which add little regulatory value (and which

[9] For non-authorised counterparties, see the FCA's powers under regulation 7 of the Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) Regulations 2013/504 to require information to determine whether they have complied with UK EMIR.

UK EMIR	Subject matter	Current position	Proposal	Comments
		basis on which the FCA may decide to give a partial approval or refuse approval). • The exemption applies to intragroup transactions between a UK NFC and a non-UK counterparty if both additional conditions below are satisfied but only if the UK NFC has notified the FCA and the FCA agrees that both additional conditions are satisfied within 3 months of the notification (this can create excessive delay for counterparties). • The two additional conditions are that: o first, there is no current or foreseen practical or legal impediment to the prompt transfer of own funds or repayment of liabilities between the counterparties; and o secondly, the risk-management procedures of the counterparties are adequately sound, robust and consistent with the level of	exemption on the same terms as UK counterparties).	do not apply to the intragroup exemption from the clearing obligation). • The proposal would end the extraterritorial application of the UK margin obligation to transactions between non-UK counterparties (which adds little regulatory value).

UK EMIR	Subject matter	Current position	Proposal	Comments
		complexity of the derivative transaction. (There is no helpful guidance on how to apply these conditions – the RTS on the first condition is unhelpful). • No exemption is available for transactions between two non-UK counterparties which are part of the same group (where the margin obligation applies to them on the basis that the transaction has a direct, substantial and foreseeable effect in the UK). • There is no procedure for counterparties to challenge an adverse decision by FCA (other than judicial review).		
Article 11(11)	Public disclosure of use of the intragroup exemption from margin requirements	• A counterparty making use of the intragroup exemption from margin requirements must make public disclosure of its use of the exemption.	• Delete public disclosure requirement. • FCA has power to require a counterparty making use of the exemption to provide information to FCA about its use of the exemption.	• Public disclosure provides little useful information to shareholders or creditors and adds little regulatory value. • The proposed new power would enable FCA to obtain information from non-authorised counterparties about the extent of the usage

UK EMIR	Subject matter	Current position	Proposal	Comments
				of the exemption (in addition to FCA's existing powers to obtain information to verify compliance with the requirements of EMIR).

Related provisions

Article	Subject matter	Current position	Proposal	Comments
Article 9(1) UK EMIR	Reporting obligation	• Transactions between members of the same group[10] are exempt from the reporting obligation if one counterparty is an NFC (or a non-UK entity that would be an NFC if established in the UK) and if the following additional conditions are satisfied: ○ both counterparties are included in the same consolidation on a full basis (based on a complex definition, which - for groups headed by a non-UK parent - partly relies on the equivalence of the relevant accounting standards used by the group); ○ both counterparties are subject to appropriate	• Transactions between members of the same group are exempt from the reporting obligation if one counterparty is an NFC (or a non-UK entity that would be an NFC if established in the UK). • The additional conditions do not apply.	• The proposal would simplify and clarify the process for firms. • FCA can rely on its existing powers to obtain information to verify compliance with the requirements of the exemption.[11] • The proposal would end the discrimination against groups headed by UK counterparties that are FCs. Note: See comments above on Article 3 UK EMIR in relation to the definition of "group".

[10] In TR Answer 51(m) of ESMA's EMIR Q&A (31 March 2021), ESMA noted the European Commission's view that the reporting exemption in Article 9(1) of EU EMIR does not cover intragroup transactions for which the parent undertaking is established in a non-EU jurisdiction. The corresponding provisions of Article 9(1) UK EMIR refer to the definition of 'group' in point (16) of Article 2(1) UK EMIR, as amended under the European Union (Withdrawal) Act 2018, which is not limited to groups headed by an undertaking established in the UK.

[11] For non-authorised counterparties, see the FCA's existing powers under regulation 7 of the Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) Regulations 2013/504 to require information to determine whether they have complied with UK EMIR.

Article	Subject matter	Current position	Proposal	Comments
		centralised risk evaluation, measurement and control procedures (but there is no clear definition of what procedures are regarded as appropriate); and o the parent undertaking is not an FC (it is not clear which parent undertaking this refers to and the condition discriminates against UK group as non-UK counterparties are not FCs). • The exemption is only available if the counterparties have notified the FCA and the FCA does not object within 3 months on the basis that the additional conditions are not satisfied. • There is no procedure for counterparties to challenge an adverse decision by FCA (other than judicial review). • Counterparties are part of the same group if they are linked by a parent-subsidiary relationship or are subsidiaries of a common parent (as defined in the Companies Act) or are		

Article	Subject matter	Current position	Proposal	Comments
		linked by a "common management relationship" (as defined in UK CRR).		
Article 28 UK MiFIR	Derivatives trading obligation (DTO)	• Transactions between UK counterparties that are FCs or NFC+s are exempt from the DTO if they are intragroup transactions within Article 3 UK EMIR. • Transactions between a UK counterparty that is an FC or NFC+ and a non-UK counterparty that would be an FC or NFC+ if established in the UK are subject to the UK DTO without an explicit exemption for intragroup transactions, but Article 3 UK EMIR only applies if an equivalence decision is in effect for non-UK jurisdiction and there is no explicit provision allowing reliance on the temporary intragroup exemption regime under SI 2019/335. • Transactions between two non-UK counterparties may be subject to the DTO if the transaction has a direct, substantial and foreseeable effect in the UK but those transactions are not	• The DTO does not apply to transactions that are not subject to the clearing obligation. ***OR*** • The DTO does not apply to transactions that are intragroup transactions which are exempt from the clearing obligation (see above). • The DTO does not apply to transactions between two non-UK counterparties (or, if it is to apply to transactions between two UK branches of non-UK FCs, those branches are allowed to rely on the exemption on the same terms as UK counterparties).	• The proposal would simplify and clarify the application of the DTO to transactions between members of the same group. • The proposal would eliminate conditions which add little regulatory value, in particular the requirement for an equivalence assessment of non-UK jurisdictions. • The proposal would align the exemption from the DTO with the exemption from the clearing obligation.

Article	Subject matter	Current position	Proposal	Comments
		intragroup transactions within the meaning of Article 3 UK EMIR. • See comments on Article 3 above for other issues with respect to the application of the definition of the intragroup exemption.		