Final Report

EMIR RTS on various amendments to the bilateral margin requirements in view of the international framework as well as on novations from UK to EU counterparties

23 November 2020| ESAs 2020 20

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Acronyms used

Bilateral margining RTS	Commission Delegated Regulation (EU) No 2016/2251 of 4 October 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty (OJ L 340, 15.12.2016, p. 9); also referred to as "Commission Delegated Regulation on bilateral margining".
CCP	Central Counterparty
EMIR	European Market Infrastructures Regulation – Regulation (EU) 648/2012 of the European Parliament and Council on OTC derivatives, central counterparties and trade repositories – also referred to as "the Regulation"
EBA	European Banking Authority
EBA Regulation	Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12)
EIOPA	European Insurance and Occupational Pensions Authority
EIOPA Regulation	Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48)
ESAs	European Supervisory Authorities, namely the EBA, EIOPA and ESMA
ESMA	European Securities and Markets Authority
ESMA Regulation	Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84)
ESRB	European Systemic Risk Board
NCA	National Competent Authority
OTC	Over-the-counter
RTS	Regulatory Technical Standards
TEU	Treaty on the European Union

1 Executive Summary

Reasons for publication

This final report presents new draft regulatory technical standards (RTS) on the risk mitigation techniques for OTC derivative contracts not cleared by a CCP (bilateral margining) that the European Supervisory Authorities (ESAs) have developed under Article 11(15) of Regulation (EU) No 648/2012 of the European Parliament and Council on OTC derivatives, central counterparties and trade repositories (EMIR). The draft RTS propose to amend Commission Delegated Regulation (EU) No 2016/2251 that sets out the detailed bilateral margin requirements.

The draft RTS relate to two main topics, the introduction of a number of amendments to the Commission Delegated Regulation on bilateral margining that take into account the international framework agreed by the Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO) and the progress made in its implementation, as well as the treatment of OTC derivative contracts novated from a counterparty established in the United Kingdom (UK) to a counterparty established in a Member State as a consequence of the withdrawal of the UK from the EU[1].

With regards to the first aspect covered in the draft RTS, i.e. the introduction of a number of amendments in view of the changes and current level of implementation of the BCBS and IOSCO framework, it can be noted that this final report is an update to the final report and the draft RTS submitted by the ESAs to the Commission and subsequently published on the websites of the ESAs on 4 May 2020 (ESAs 2020 09). Taking into account further considerations with respect to OTC derivative intragroup transactions as well as to equity option transactions, the previous version of the Final Report from May was further reviewed and updated, leading to this new version of the Final Report on the draft RTS on bilateral margining. This updated version of the Final Report thus replaces entirely the version previously submitted to the Commission in May 2020.

As a reminder on what was already covered in the May version of the Final Report, in view of the progress made globally towards the implementation of the international BCBS and IOSCO framework, stakeholders have asked for a number of adjustments in the EU legislative rulebook in order to better facilitate international consistency. These relate to the treatment of physically settled FX forward and swap contracts, intragroup contracts, equity

[1] Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community (OJ C 384 I, 12.11.2019, p. 1).

option contracts and the implementation of the initial margin requirements. The ESAs' proposal includes amendments of the Commission Delegated Regulation on bilateral margining in order to facilitate further international consistency towards the implementation of the international framework.

With regards to the second aspect covered in the draft RTS, the treatment of OTC derivative contracts novated from a counterparty established in the United Kingdom (UK) to a counterparty established in the EU, the provisions have been developed following a similar reasoning as with:

- Commission Delegated Regulation (EU) No. 2019/397 based on the draft RTS developed jointly by the ESAs and submitted to the European Commission on 28 November 2018, which were endorsed by the European Commission on 19 December 2018 and which were published in the Official Journal on 13 March 2019 ('the first Delegated Regulation'), and

- Commission Delegated Regulation (EU) 2019/564, dated 28 March 2019 and published in the Official Journal on 10 April 2019 (the 'second Delegated Regulation').

The application of the above two Delegated Regulations was conditional. However, as a result of (i) for the first Delegated Regulation, the decision of the European Council of 21 March 2019 to extend the two-year period referred to in Article 50(3) of the Treaty on European Union ('TEU') following a request from the UK, and (ii) for the second Delegated Regulation, the withdrawal agreement signed on 24 January 2020 with regards to the conditions for the UK's departure from the EU (which entered into force on 1 February 2020 and which introduced a transition period running until 31 December 2020), none of them has applied.

The UK informed the EU on 12 June 2020 that an extension of the transition period would not be sought and thus such an extension is not envisaged. The probability of having a scenario where no agreement, which would cover the above-mentioned issues, is reached before the end of the transition period is very high, and therefore the reasons underlying the first two abovementioned Delegated Regulations remain valid today. ESMA hereby proposes a new amending RTS mirroring the content of Commission Delegated Regulations 2019/397 and 2019/564, that takes into account this new situation.

In the context of the withdrawal of the UK from the EU, stakeholders have asked for a general grandfathering for legacy OTC derivative contracts between UK and EU counterparties, but the ESAs do not consider it to be appropriate to provide for a general grandfathering and it is not in their mandate.

However the ESAs consider it to be appropriate to preserve the characteristics of contracts for which bilateral margins were not required, and which contracts are subsequently novated from one counterparty established in the UK to another counterparty established in a Member State, in order to address the situation whereby the original UK counterparty may no longer be able to provide certain services across the EU after the end of the transition period.

The ESAs' proposal includes an amendment of the Commission Delegated Regulation on bilateral margining in order to facilitate certain Brexit-related novations of contracts to EU counterparties during a specific time-window.

The proposed amendments are an adaptation of the timelines and rules to facilitate the current implementation of the Commission Delegated Regulation on bilateral margining, and more broadly of the international framework, and each of the proposed amendments are limited in nature. Moreover, some of the deadlines related to these provisions have passed or are due to expire soon. It could also be noted that the measures regarding the novation of contracts from UK counterparties to EU counterparties had already been adopted but never took effect, whereas the same reasoning for which they were adopted the first time is still valid, and are thus simply reintroduced in this report. In addition, there is urgency to provide this regulatory solution in order to facilitate the transfer of contracts to counterparties located in the EU in view of the upcoming end of the transition period. Therefore, with a view to provide clarity as soon as possible on the overall timelines regarding the implementation of the bilateral margin requirements, to facilitate as soon as possible a consistent implementation of the BCBS and IOSCO framework and to provide this regulatory solution for the transfer of contracts to counterparties located in the EU, in accordance with Article 10(1) of the EBA, EIOPA and ESMA Regulations respectively, the ESAs have not conducted any open public consultation. However, the stakeholder groups of each of the ESAs have been consulted for the previous version of this Final Report and have been informed of this new version.

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This Report provides explanations on the draft RTS amending the current Commission Delegated Regulation on bilateral margining with respect to the treatment of physically settled FX forward and swap contracts, intragroup contracts, equity option contracts and the implementation of the initial margin requirements, as well as with respect to the treatment of novated contracts from a counterparty established in the UK to a counterparty which is established in a Member State.

Next Steps

This Final Report is sent to the European Commission, and the ESAs are submitting the draft technical standards presented in Annex for endorsement, in the form of a Commission Delegated Regulation, i.e. a legally binding instrument applicable in all Member States of the European Union. Following the endorsement, they are then subject to non-objection by the European Parliament and the Council.

The ESAs cannot disapply EU law. However, in view of the remaining steps mentioned above that the draft RTS need to go through before being finalised and to enter into force, and in light of some of the relevant deadlines, with regards to the bilateral margin requirements and the treatment of physically settled FX forward and swap contracts, intragroup contracts, equity option contracts, the implementation of the last phases of the initial margin requirements as well as the end of the transition period with the UK and the treatment of OTC derivative contracts novated from the UK to the EU, the ESAs expect competent authorities to apply the EU framework in a risk-based and proportionate manner with regards to the requirements related to the measures contained in the draft RTS until the amended RTS enter into force.

2 Final report

2.1 Introduction

1. The BCBS and IOSCO designed and agreed international standards for the exchange of bilateral margin along with a calendar to facilitate a consistent implementation across jurisdictions. In particular, this international framework contains a phase-in for the implementation of the initial margin requirements which has been spread over several years and this implementation is still ongoing.

2. These international standards have been implemented in the EU regulatory framework through Commission Delegated Regulation (EU) No 2016/2251 on bilateral margining. Indeed, the ESAs, who have a joint mandate under Article 11(15) of EMIR, have developed RTS taking into account the international framework, and the Commission Delegated Regulation on bilateral margining is based on these RTS.

3. Following the agreed calendar of the international framework, the Commission Delegated Regulation on bilateral margining contains a phase-in for a range of requirements, including various deferred dates of application for certain contracts or counterparties, in order to facilitate international consistency in the implementation of these standards. This reflects the strong belief of the ESAs that, in the area of the margining of non-centrally cleared OTC derivatives, a global level playing field is necessary, such that regulatory competition and a 'race to the bottom' are avoided.

4. The Commission Delegated Regulation on bilateral margin requirements was adopted by the European Commission on 4 October 2016, and then following a period of non-objection by the European Parliament and Council it was published in the Official Journal on 15 December 2016, which triggered the start of the implementation of the requirements in the EU.

2.2 International framework and progress in its implementation

2.2.1 Background

5. Since the entry into force of the Commission Delegated Regulation on bilateral margining, in parallel to similar efforts in other jurisdictions, the ESAs have monitored the implementation of these requirements in the EU, and by the regulatory community at the global level, including the BCBS and IOSCO as well as the Financial Stability Board (FSB). This monitoring has confirmed overall progress towards the implementation of the standards but has also highlighted

certain areas where further consistency could be facilitated, or areas where the requirements could be clarified or slightly amended in order to facilitate their implementation.

6. Some of these areas have led the BCBS and IOSCO to clarify or slightly amend the international framework, others concern adjustments needed to ensure a level playing field.

7. Following the above, the ESAs reviewed in 2019 the application of the relevant requirements of the Commission Delegated Regulation on bilateral margining and identified a number of amendments to be introduced that were presented in a first version of this Final Report, which was submitted to the Commission and published on the websites of the ESAs on 5 December 2019.

8. However, a few months later, in response to the Covid-19 outbreak, the BCBS and IOSCO agreed and communicated on 3 April 2020 the deferral by one year of the implementation of the remaining phases of the initial margin requirements. The Final Report was updated to take into account the new BCBS and IOSCO decision for a deferral. This second version of the Final Report on the draft RTS on bilateral margining was submitted to the Commission and published on the websites of the ESAs on 4 May 2020.

9. Lastly, in view of the overall context this year, the draft RTS were reviewed once more and the Final Report was updated again, this time with respect to the exemption for OTC derivative intragroup transactions and the exemption for equity options, in order to avoid undue costs and to ensure a level playing field. This new and third version of the Final Report on the draft RTS on bilateral margining thus replaces entirely the two versions previously submitted to the Commission and published on the websites of the ESAs on 5 December 2019 and 4 May 2020 respectively.

10. The next section describes these different areas in detail.

2.2.2 Proposed amendments and clarifications

2.2.2.1 Clarification of the requirements when below the 50 million initial margin threshold

11. In September 2018, several trade associations sent a letter to the BCBS and IOSCO, about the implementation issues relating to the remaining phases of implementation of the initial margin requirements, arguing in particular that there is a bottleneck issue due to the large number of counterparties caught in the last phase whereas many of them would not pose a material systemic risk, and thus raising the need to review the requirements and the ongoing implementation.

12. Following an analysis of the issue, the BCBS and IOSCO issued a first clarification in March 2019 that did provide a significant level of relief to a very large number of counterparties expected to be in scope in the last phase, while not affecting the requirements contained in the international standards. Hence, it was a clarification on the existing rule and it did not require a change in the international framework:

    "In the remaining phases of the framework's implementation in 2019 and 2020, initial margin requirements will apply to a large number of entities for the first time, potentially involving documentation, custodial and operational arrangements. The Basel Committee and IOSCO note that the framework does not specify documentation, custodial or operational requirements if the bilateral initial margin amount does not exceed the framework's €50 million initial margin threshold. It is expected, however, that covered entities will act diligently when their exposures approach the threshold to ensure that the relevant arrangements needed are in place if the threshold is exceeded."

13. The ESAs have reviewed the application of the relevant requirements of Commission Delegated Regulation on bilateral margining and are of the view that that clarification can already be taken into account when applying them. Thus, the ESAs consider that there is no need to amend the Delegated Regulation on bilateral margin requirements in order for counterparties below the 50 million initial margin exchange threshold not to be required to have all the relevant operational and legal arrangements in place. No amendment related to this point is thus included in the draft RTS in Annex.

2.2.2.2 Extension of the phase-in of the implementation of the initial margin requirements

A. Introduction of an additional implementation phase

14. Still, in relation to the implementation challenges raised by several trade associations mentioned in the previous point, the BCBS and IOSCO have analysed in more detail the issues around the last phase-in of the requirements and have indicated in July 2019 to having agreed to an extension of this phase-in:

    "The Basel Committee and IOSCO have agreed to extend by one year the final implementation of the margin requirements. With this extension, the final implementation phase will take place on 1 September 2021, at which point covered entities with an aggregate average notional amount (AANA) of noncentrally cleared derivatives greater than €8 billion will be subject to the requirements. To facilitate this extension, the Basel Committee and IOSCO also will introduce an additional implementation phase whereby as of 1 September 2020 covered entities with an AANA of non-centrally cleared derivatives greater than €50 billion will be subject to the requirements.

The Basel Committee and IOSCO have agreed to this extended timeline in the interest of supporting the smooth and orderly implementation of the margin requirements which is consistent and harmonised across their member jurisdictions and helps avoid market fragmentation that could otherwise ensue. The Basel Committee and IOSCO expect that covered entities will act diligently to comply with the requirements by this revised timeline and strongly encourage market participants to make all relevant arrangements on a timely basis."

15. Following from this, the ESAs have reviewed the Commission Delegated Regulation on bilateral margining and have identified the amendments necessary to the EU framework in order to extend the implementation deadline by one year for those counterparties above the 8 billion threshold but below the new 50 billion threshold.

16. It can also be noted that no further amendment of the framework, except for the deferral introduced in response to the Covid-19 outbreak presented in section B below, and more specifically no further extension of the phase-in and no change of the thresholds, in particular the 8 billion threshold, are envisaged. As a result, it is important that the counterparties who have been facing some challenges in their preparation for complying with the initial margin requirements and that under the proposed draft RTS would have some additional time to complete them, continue their preparation efforts in order to be able to comply by the deadline.

B. Deferral in response to the Covid-19 outbreak

a. New version of the Final Report and draft RTS

17. As explained in the Background section 2.1, a first version (ESAs 2019 20) of this Final Report had been submitted to the Commission and published on the websites of the ESAs on 5 December 2019. Indeed, the ESAs had completed in December 2019 the review of the application of the relevant requirements of the Commission Delegated Regulation on bilateral margining to take into account the latest changes to the international framework and the level of progress in its implementation, at that time.

18. However, in response to the Covid-19 outbreak in 2020, the Final Report has been updated to take into account the related decision from the BCBS and IOSCO communicated on 3 April 2020 to defer the implementation of the remaining phases of the initial margin requirements. In terms of substance, the resulting targeted update of the Final report has been centered on the introduction of this new section 2.2.2 B and the related change to the draft RTS with respect to the applicable deadlines.

19. This updated version of the Final Report on the draft RTS on bilateral margining thus replaces entirely the version submitted to the Commission in December 2019.

b. Regulatory response to enable additional operational capacity

20. In response to the COVID-19 outbreak in 2020, the ESAs have intensified their coordination with NCAs, as well as with relevant authorities from other jurisdictions in order to ensure adequate regulatory actions where needed. This has led in particular to a number of clarifications on the applicable requirements or deadlines, which now include margin requirements for non-centrally cleared OTC derivatives.

21. In this context, in view of the broad range of issues that market participants are dealing with following the Covid-19 outbreak, the BCBS and IOSCO have taken account of the challenges they would face in their preparations for the remaining phases of the implementation of the requirements, and have indicated on 3 April 2020[2] to having agreed to an extension of this phase-in:

> "The Basel Committee on Banking Supervision (BCBS) and the International Organization of Securities Commissions (IOSCO) continue to monitor the impact of the rapid spread of the coronavirus disease (Covid-19) on the global financial system. In light of the significant challenges posed by Covid-19, including the displacement of staff and the need for firms to focus resources on managing risks associated with current market volatility, BCBS and IOSCO have agreed to extend the deadline for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives, by one year. This extension will provide additional operational capacity for firms to respond to the immediate impact of Covid-19 and at the same time, facilitate covered entities to act diligently to comply with the requirements by the revised deadline.
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> With this extension, the final implementation phase will take place on 1 September 2022, at which point covered entities with an aggregate average notional amount (AANA) of non-centrally cleared derivatives greater than €8 billion will be subject to the requirements. As an intermediate step, from 1 September 2021 covered entities with an AANA of non-centrally cleared derivatives greater than €50 billion will be subject to the requirements."

22. Following on from this, the ESAs have reviewed the application of the relevant requirements of Commission Delegated Regulation (EU) No 2016/2251 on bilateral margining and the amending draft RTS submitted in December 2019, and have identified the amendments necessary in order to extend the implementation

[2] Link to the BCBS and IOSCO statement from 3 April 2020: https://www.iosco.org/news/pdf/IOSCONEWS560.pdf

deadlines by one year for those counterparties in the final two phases. The draft RTS in Annex integrates the further phase-in described in both sections 2.2.2 A and B.

23. Lastly, it should also be remembered that these draft RTS are still subject to endorsement by the European Commission and a non-objection period by the European Parliament and Council, and thus legal certainty on the further phase-in described in section 2.2.2 and proposed by the ESAs would only be confirmed after these steps and the publication in the Official Journal.

2.2.2.3 Physically settled FX Forwards and Swaps

24. The international framework gives explicit guidance on physically settled FX forwards and swaps:

> "BCBS and IOSCO agree that standards apply for variation margin to be exchanged on physically settled FX forwards and swaps in a manner consistent with the final policy framework set out in this document and that those variation margin standards are implemented either by way of supervisory guidance or national regulation."

25. The international standards state that variation margining of physically settled FX forwards and swaps is both an established practice among significant market participants and a prudent risk management tool that limits the build-up of systemic risk, and thus that variation margining should apply to these contracts.

26. The international standards recommend implementing this requirement by way of national regulation or supervisory guidance. The EU initially implemented these international standards by way of regulation. Specifically, this was done through Article 27(a) of Commission Delegated Regulation on bilateral margining, which exempts these contracts from the exchange of initial margin, in line with the international framework, and through Article 37(2) thereof for the variation margin requirements, including a deferred date of application for physically settled FX forwards until 3 January 2018, which is the date of application of the revised Markets in Financial Instruments Directive (MiFID II)[3] and thus when the definition of physically settled FX forwards was further harmonised.

27. Although the bilateral margin requirements for physically settled FX forwards were meant to apply from the entry into force of MiFID II at the start of January 2018, market participants raised some concerns which the ESAs analysed.

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[3] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, OJ L 173, 12.6.2014, p. 349–496.

28. Based on the material presented to the ESAs, it became apparent that the adoption of the international standards in other jurisdictions via supervisory guidance had led to an international scope of application that is more limited than the scope the ESAs had proposed in the RTS (and which was finally embedded in the EU rules). Whereas the requirement remains relevant for transactions between institutions, the implementation appeared to pose a challenge regarding transactions between institutions and end-users.

29. Following from this, the ESAs developed and submitted in December 2017 a joint RTS on bilateral margining with respect to physically settled FX forward contracts, that proposed a permanent exemption for certain contracts when entered into between institutions and end-users. It can be noted though that the process for the proposed amending RTS from December 2017 has not been completed and thus that it has not become law. However, the ESAs are of the view that the rationale for the proposed amendment is still valid.

30. More recently, following the EMIR Review, the co-legislators have agreed on a range of amendments to EMIR in Regulation (EU) 2019/834, also referred to as the EMIR Refit text[4]. The EMIR Refit text was published on 28 May 2019 and entered into force on 17 June 2019. It is important to note in this context that the co-legislators have reiterated through the EMIR Refit text the importance of international consistency in the implementation of the international standards on bilateral margining, and in particular with regards to the treatment of physically settled FX forwards and swaps. Recital 21 of the EMIR Refit text makes clear that:

> "The need for international regulatory convergence and the need for non-financial counterparties and small financial counterparties to reduce the risks associated with their currency risk exposures make it necessary to set out special risk-management procedures for physically settled foreign exchange forwards and physically settled foreign exchange swaps. In view of their specific risk profile, it is appropriate to restrict the mandatory exchange of variation margins on physically settled foreign exchange forwards and physically settled foreign exchange swaps to transactions between the most systemic counterparties in order to limit the build-up of systemic risk and to avoid international regulatory divergence."

31. Following from this, the ESAs have discussed with the European Commission the need to replace the amendment submitted by the ESAs in December 2017 by a new amendment covering a broader scope, i.e. not only covering physically settled

[4] Regulation (EU) 2019/834 of the European Parliament and the Council of 20 May 2019 amending Regulation (EU) No 648/2012 as regards the clearing obligation, the suspension of the clearing obligation, the reporting requirements, the risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty, the registration and supervision of trade repositories and the requirements for trade repositories (Text with EEA relevance). OJ L 141, 28.5.2019, p.42.

FX forwards, but covering both physically settled FX forwards and swaps, with the same exemption for both. The draft RTS included in Annex contains this broader scope.

2.2.2.4 Temporary exemption for single-stock equity options and index options

32. As described above, the Commission Delegated Regulation on bilateral margining contains a range of implementation timelines, including a phase-in for the initial margin requirements as well as deferred dates of application for certain contracts and counterparties. In particular, the requirements for single-stock equity options or index options transactions have been deferred until 4 January 2020 in the Commission Delegated Regulation on bilateral margining.

33. Recital 43 of the Commission Delegated Regulation on bilateral margining provides the rationale behind the initial three-year temporary exemption, it states that:

> "In order to avoid market fragmentation and ensure a level playing field for Union counterparties established in the Union on a global level, and acknowledging the fact that in some jurisdictions the exchange of variation and initial margin for single-stock options and equity index options is not subject to equivalent margin requirements, the treatment of those products should be phased-in. This phase-in period will provide time for monitoring regulatory developments in other jurisdictions and ensuring that appropriate requirements are in place in the Union to mitigate counterparty credit risk in respect of such contracts whilst avoiding scope for regulatory arbitrage."

34. Three years later, the situation had not materially changed. Certain jurisdictions had not implemented these requirements for these contracts or had also introduced temporary exemptions in the meantime.

35. The ESAs reiterate the view that, from a prudential point of view, the international framework agreed on by all the participant authorities in the BCBS and IOSCO discussions is a crucial pillar in ensuring safer derivatives markets, limiting the counterparty risk between counterparties trading derivatives, and thus that its coordinated implementation is key in reaching this objective.

36. Furthermore, the same Recital 21 of the EMIR Refit text that is mentioned in the section on physically settled FX forwards and swaps also comes in support of this objective of an implementation of the international framework across the range of derivatives. Recital 21 states that:

> "International regulatory convergence should also be ensured with regard to risk-management procedures for other classes of derivatives."

37. With the view to continue monitoring regulatory developments in other jurisdictions and ensuring that appropriate requirements are in place in the Union to mitigate counterparty credit risk in respect of such contracts whilst avoiding scope for regulatory arbitrage, when conducting the review of the RTS in 2019, it appeared proportionate to the ESAs to propose to extend by one year the current deferred application of the margin requirements for single-stock equity options or index options transactions in the EU framework. The draft RTS submitted in December 2019 and again in May 2020 thus contained this proposal.

38. However, a few months later, especially in the current context, it seems unlikely that the jurisdictions initially considered by the ESAs would move anytime soon towards more regulatory convergence with regard to equity options, making the reasons described above for the initial exemption and the subsequent extension relevant again

39. Therefore, and in line with the call from the co-legislators expressed in the above-cited EMIR Refit Recital that international regulatory convergence should also be ensured with regard to risk-management procedures for other classes of derivatives, it would appear appropriate to introduce at this stage an extension of the temporary exemption for equity options.

40. Following from this, the ESAs have discussed with the European Commission the need to replace the amendment submitted by the ESAs in December 2019, and again in May 2020, by a new amendment to extend the temporary exemption for equity options by three more years. The draft RTS included in Annex contain this proposed amendment.

2.2.2.5 Temporary exemption for intragroup transactions

41. Another deferred date of application of the bilateral margin requirements relates to intragroup transactions with a third country entity in the absence of an equivalence decision adopted by the European Commission pursuant to Article 13(2) of EMIR. The requirements for these intragroup transactions are currently deferred until 4 January 2020 in the Commission Delegated Regulation on bilateral margining.

42. ESMA already looked at this question from the perspective of the clearing obligation. After running a consultation, ESMA finalised and submitted a draft RTS to the European Commission on 27 September 2018 proposing to extend the

temporary regime by two years until 21 December 2020. The draft RTS have since been endorsed, then published in the Official Journal and have entered into force[5].

43. The rationale for the exemption from the clearing obligation is the same as for the exemption from the bilateral margin requirements, i.e. broadly speaking that those deferred dates were necessary to ensure that such intragroup OTC derivate contracts were not subject to the EMIR clearing or bilateral margin requirements before the adoption of the relevant equivalence decisions.

44. At the time of the first Final Report (and the situation was the same at the time of the second Final Report), only two equivalence decisions had been adopted (the US CFTC in 2017 and Japan in 2018). The ESAs were thus of the view that in light of this common rationale for a temporary exemption, it was proportionate to also extend the temporary exemption for bilateral margin and to align it with the exemption for the clearing obligation, i.e. until 21 December 2020. The draft RTS submitted in December 2019 and again in May 2020 thus contained such proposal.

45. A few months later, the situation is still the same (only the same two equivalence decisions regarding the regimes of the US CFTC[6] and Japan[7]) and the deadline resulting from the previously proposed extension, 21 December 2020, is now getting closer. Although a batch of equivalence decisions could still be possible in time for the end of the deferral, there is a risk that these decisions could in fact not be adopted in time and that the scope of this batch would not be sufficient for EU firms to properly manage their intragroup risk management. This would thus limit the ability of some EU counterparties to properly manage their intragroup risk management.

46. At this stage, subjecting EU counterparties to intragroup margin requirements for certain of their intragroup OTC derivative transactions by 21 December 2020 would be operationally difficult, would add undue costs and introduce a level playing field issue for EU counterparties.

47. Following from this, the ESAs have discussed with the European Commission the need to replace the amendment submitted by the ESAs in December 2019, and again in May 2020, by a new amendment to extend the deferred date of application to 30 June 2022. The draft RTS included in Annex contains this proposed amendment.

[5] Commission Delegated Regulation (EU) 2019/667 of 19 December 2018 amending Delegated Regulations (EU) 2015/2205, (EU) 2016/592 and (EU) 2016/1178 to extend the dates of deferred application of the clearing obligation for certain OTC derivative contracts (Text with EEA relevance). OJ L 113, 29.4.2019, p. 1–3.
[6] OJ L 265, 14.10.2017, p. 23–27.
[7] OJ L 115, 2.5.2019, p. 11–15.

48. It should also be noted that a similar amendment is being considered in parallel by ESMA with regards to the temporary exemption from the clearing obligation for OTC derivative intragroup transactions.

2.3 Novations from UK counterparties to EU counterparties

2.3.1 Background

49. As explained in the Final Report related to the first Delegated Regulation on the treatment of OTC derivative contracts novated from a counterparty established in the UK to a counterparty established in the EU (Delegated Regulation (EU) 2019/397), in the context of the withdrawal of the UK from the EU, stakeholders have asked for a general grandfathering for OTC derivative contracts, and an exemption from certain requirements stemming from EMIR.

50. When EU law would cease to apply post-withdrawal and once the transition period has ended, counterparties established in the UK will no longer be able to provide investment services in the EU under the current passporting regime, so they might not be in a position to execute certain operations in relation to derivative contracts they have with EU clients, in particular certain so-called “life-cycle events” that can be construed in certain jurisdictions as the entering into new transactions (such as novations, unwinding by entering into an offsetting transaction, compression with new replacement contracts, etc.).

51. This means that after the withdrawal of the UK from the EU and the end of the transition period, the performance of certain restructuring operations on certain contracts could require authorisation in some Member States, in line with national third country regimes. Those counterparties established in the UK would then face 27 national third country regimes.

52. In order to address this situation, these counterparties might have to novate their contracts to counterparties established in the EU, which would benefit from the single passport in financial services.

53. However, the resulting new contracts might be subject to new obligations that were not applicable at the time the original contracts were signed and for which, in the absence of such withdrawal, they might have continued enjoying an exemption (please see the Section on the rationale for the proposed amendments below for more details).

54. This would represent a clear disincentive to transfer contracts to firms established in the EU and the ESAs have thus considered some actions aiming at facilitating the transfer of contracts by the private sector to counterparties established in the

EU (please see the Section on the proposed amendments below for more details), to ensure that the regulatory characteristics of the original contracts are preserved. Indeed, the ESAs would like to stress again the need and importance for counterparties to prepare for when the transition period ends, which could include a number of actions, including this potential transfer of contracts.

2.3.2 Rationale

55. This final report focuses on bilateral non-centrally cleared OTC derivative contracts currently benefitting or that would benefit from the grandfathering arrangements under EMIR, i.e. contracts in respect of which, to this date, parties did not have to apply the new procedures on the exchange of collateral (bilateral margins), either because the relevant dates set out in Commission Delegated Regulation on bilateral margining had not applied yet, or because the contracts have not been novated after those dates (often referred to as "legacy contracts").

56. If, due to the withdrawal from the EU of the UK in which one of the counterparties is established, the parties decide to novate their legacy contracts from that counterparty to a new counterparty established in the EU, the novation of the contracts will trigger the requirements for the bilateral margin procedures and the related margining requirements referred to in Article 36 to 38 of Commission Delegated Regulation (EU) No 2016/2251, if such novation occurs after the relevant dates of application specified in these articles for that type of contract. As a result, the parties will have to apply the bilateral margin procedures and the related margining requirements.

57. Therefore, the novation of such legacy contracts in the EU would make, *ceteris paribus*, the overall performance of the contracts costlier for the parties, due to the application of the EMIR margining requirements.

58. Given that these shortcomings are a direct consequence of the withdrawal of the UK from the EU, an event that is beyond the control of the parties, and that this may put the EU counterparties facing UK counterparties at a disadvantage compared to EU counterparties facing other EU counterparties, the ESAs consider that it is relevant to maintain a level playing field and are proposing amendments to the existing Commission Delegated Regulation on bilateral margining that would allow these counterparties to novate their contracts to EU counterparties without triggering the EMIR margining requirements.

2.3.3 Renewed need for amendments

59. This situation was first addressed in late 2018 and in the first part of 2019 when the UK was expected to leave the EU in March 2019 and then in April 2019. Indeed,

ESMA developed a first draft RTS in relation to this issue, which was submitted[8] to the European Commission on 28 November 2018, and which were endorsed by the European Commission on 19 December 2018. Commission Delegated Regulation (EU) No.2019/397, based on the draft RTS developed by ESMA, was then published in the Official Journal[9] on 13 March 2019.

60. The application of this first Delegated Regulation was conditional. One of the conditions for the application of the first RTS was that a decision had not been taken to extend the two-year period referred to in Article 50(3) of the Treaty on European Union ('TEU') and it did therefore not apply following the decision of the European Council of 21 March 2019 to extend that period following a request from the UK.

61. Nevertheless, the reasons underlying the first Delegated Regulation remained and thus a second Delegated Regulation was adopted, Commission Delegated Regulation (EU) No. 2019/564, dated 28 March 2019, was published in the Official Journal on 10 April 2019[10]. It mirrored the content of the first Delegated Regulation but amending the condition related to the extension of the two-year period referred to in Article 50(3) of the TEU.

62. One of the conditions for the application of the second Delegated Regulation was that no withdrawal agreement concluded with the UK in accordance with Article 50(2) of the TEU would have entered into force by the date the UK would have left the EU.

63. The Withdrawal Agreement was signed on 24 January 2020 and entered into force on 1 February 2020 with regards to the conditions for the UK's departure from the EU and introduced a transition period until 31 December 2020. It entered into force as of the following day after the UK left the EU on 31 January 2020. Therefore, the second Delegated Regulation did not become applicable.

64. The UK informed the EU on 12 June 2020 that an extension of the transition period would not be sought and thus such an extension is not envisaged. However, the reasons underlying the first two Delegated Regulations mentioned above remain. The ESAs therefore propose in this new Final Report new provisions mirroring the

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[8] Link to the Final report: https://esas-joint-committee.europa.eu/Publications/Reports/ESAs%202018%2025%20-%20Final%20Report%20-%20Bilateral%20margining%20(novation).pdf

[9] Commission Delegated Regulation (EU) 2019/397 of 19 December 2018 amending Delegated Regulation (EU) 2016/2251 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council as regards the date until which counterparties may continue to apply their risk-management procedures for certain OTC derivative contracts not cleared by a CCP, OJ L 71, 13.3.2019, p. 15–17.

[10] Commission Delegated Regulation (EU) 2019/564 of 28 March 2019 amending Delegated Regulation (EU) 2016/2251 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council as regards the date until which counterparties may continue to apply their risk-management procedures for certain OTC derivative contracts not cleared by a CCP, OJ L 99, 10.4.2019, p. 3–5.

content of Commission Delegated Regulations (EU) 2019/397and 2019/564 that take into account the new situation.

2.3.4 Proposed amendments

65. For bilateral margining, EMIR Level 1 and Level 2 create the following main categories of requirements, depending on the date of conclusion (or novation) of the relevant non-centrally cleared OTC derivative contract:

    a. For contracts concluded before 16 August 2012, no requirement applies;

    b. For contracts concluded between 16 August 2012 and the relevant dates of application set out in Articles 36 to 38 of the Commission Delegated Regulation on bilateral margining, parties shall continue to apply the risk-management procedures they had in place at the date of entry into force of the Commission Delegated Regulation (Article 35 of the same Commission Delegated Regulation), which, in some instances, may well require no exchange of collateral;

    c. For contracts concluded after the dates referred to in Articles 36 to 38 of Commission Delegated Regulation on bilateral margining, parties shall apply the risk-management procedures for the exchange of variation and initial margins set out in that Commission Delegated Regulation.

66. The ESAs had investigated, in the Final Report of 28 November 2018, the possibility to set out an exemption from the application of the bilateral margin procedures and the related margining requirements under EMIR, which would create a time-window to relocate trades in the EU27 without triggering the relevant EMIR obligations. In view of the similar issue to address and building on this first set of RTS, this final report thus contains ta similar set of proposed amendments to the Commission Delegated Regulation on bilateral margining.

67. The ESAs proposal is again to create *de facto:*

    a. a new transversal sub-category of contracts, comprised of those in respect of which either no bilateral margining requirement (variation and/or initial margin, as applicable) is applicable at the date of entry into force of this amending regulation, or those in respect of which parties are permitted to continue applying their own risk-management requirements, because entered into or novated before the relevant dates (see point (a) of proposed Article 35, second paragraph), and

    b. a time window for the counterparties to novate such contracts to a counterparty established in the EU without triggering the application of the bilateral margin procedures and the related margining requirements (see point (b) of proposed Article 35, second paragraph).

68. Nonetheless, this exemption should not allow parties to fully restructure their transactions to take advantage of a pure business opportunity without ever being subject to the EMIR bilateral margining requirements. To this end, such exemption is proposed:

    a. For a limited scope: it would only apply to the novation from a UK to an EU counterparty, which would not trigger the bilateral margin procedures and the related margining requirements, and would not extend to other life-cycle events performed by the parties in relation to such contract, and

    b. For a limited period of time, which we have defined as going from the date of application of this amending regulation until twelve months after that date, in order to allow for the repapering.

69. In order to benefit from this exemption, parties should thus start negotiating the novations of their transactions which are in the scope of this amending regulation as soon as possible, given the limited time period to benefit from it. Should the parties agree on the terms of a novation before the date of application of this amending regulation, they should provide that these novations would take effect only upon the date of application of this amending regulation to benefit from the exemption.

2.4 Way forward

70. From a process point of view, it is important to note that the adjustments introduced in the proposed draft RTS are limited in nature. They are also in line with the international framework and take into account the status of the implementation of this framework at the international level which has also been documented and analysed.

71. In addition, some of the deadlines have already passed (such as the one in relation to FX derivatives), or were soon approaching at the time of the first submission of this Final Report in December 2019 , in particular the deferred date of application for intragroup transactions as well as for equity options, which was 4 January 2020. Similarly, there is urgency to provide this regulatory solution in order to facilitate novations from UK counterparties to EU counterparties and to reduce some of the legal uncertainty attached to the situation described in this document, given that the transition period is due to expire on 31 December 2020.

72. Furthermore, market participants would benefit in knowing as early as possible on whether and how to prepare for these requirements. Finally, many of these changes have also been called for by a large range of market participants.

73. As a result, the ESAs are of the view that it would be disproportionate to conduct open public consultations and analyses of the potential related costs and benefits, taking into account the scope and impact of the changes concerned in the draft RTS and the urgency of the matter for some of the requirements. Therefore, in accordance with Article 10(1) of the EBA, EIOPA and ESMA Regulations, the ESAs have not conducted any open public consultation. However, the stakeholder groups of each of the ESAs have been consulted for the previous version of this Final Report and have been informed of this new version.

74. These amendments are thus submitted directly to the European Commission for review and endorsement. The process that follows the adoption of draft RTS by the European Commission without significant amendments is a review period by the European Parliament and Council before they can then be published in the Official Journal and subsequently enter into force.

75. The ESAs cannot disapply EU law. However, in view of the remaining steps that the draft RTS need to go through before being finalised and entering into force, and in light of some of the relevant deadlines, with regards to the bilateral margin requirements and the treatment of physically settled FX forward and swap contracts, intragroup contracts, equity option contracts, the implementation of the phase-in of the initial margin requirements as well as the end of the transition period with the UK and the treatment of OTC derivative contracts novated from the UK to the EU, the ESAs expect competent authorities to apply the EU framework in a risk-based and proportionate manner with regards to the requirements related to the measures contained in the draft RTS until the amended RTS enter into force.

3 Annexes

3.1 Annex I - ESAs mandate to develop draft technical standards

Article 11(15) of Regulation (EU) No 648/2012

Risk-mitigation techniques for OTC derivative contracts not cleared by a CCP

In order to ensure consistent application of this Article, the ESAs shall develop common draft regulatory technical standards specifying:

(a) the risk-management procedures, including the levels and type of collateral and segregation arrangements referred to in paragraph 3;

(aa) the supervisory procedures to ensure initial and ongoing validation of those risk-management procedures;

(b) the procedures for the counterparties and the relevant competent authorities to be followed when applying exemptions under paragraphs 6 to 10;

(c) the applicable criteria referred to in paragraphs 5 to 10 including in particular what is to be considered as a practical or legal impediment to the prompt transfer of own funds and repayment of liabilities between the counterparties.

The level and type of collateral required with respect to OTC derivative contracts that are concluded by covered bond entities in connection with a covered bond, or by a securitisation special purpose entity in connection with a securitisation within the meaning of this Regulation and meeting the conditions of Article 4(5) of this Regulation and the requirements set out in Article 18, and in Articles 19 to 22 or 23 to 26 of Regulation (EU) 2017/2402 (the Securitisation Regulation) shall be determined taking into account any impediments faced in exchanging collateral with respect to existing collateral arrangements under the covered bond or securitisation.

The ESAs shall submit those draft regulatory technical standards, except for those referred to in point (aa) of the first subparagraph, to the Commission by 18 July 2018.

EBA, in cooperation with ESMA and EIOPA, shall submit the draft regulatory technical standards referred to in point (aa) of the first subparagraph to the Commission by 18 June 2020.

Depending on the legal nature of the counterparty, power is delegated to the Commission to adopt the regulatory technical standards referred to in this paragraph in accordance with Articles 10 to 14 of Regulations (EU) No 1093/2010, (EU) No 1094/2010 or (EU) No 1095/2010.

3.2 Annex II - Draft technical standards

COMMISSION DELEGATED REGULATION (EU) No …/..

amending Delegated Regulation (EU) 2016/2251 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regards to regulatory technical standards on the timing of when certain risk management procedures will start to apply for the purpose of the exchange of collateral

of [ ]

(text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories[11], and in particular Article 11(15) thereof,

Whereas:

(1) Commission Delegated Regulation (EU) 2016/2251[12] specifies, among others, the risk-management procedures, including the levels and type of collateral and segregation arrangements referred to in Article 11(3) of Regulation (EU) 648/2012, that financial counterparties are required to have for the exchange of collateral, with respect to their OTC derivative contracts not cleared by a central counterparty. Delegated Regulation (EU) 2016/2251 implements the international framework for the exchange of collateral that has been agreed at the global level by the Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO).

(2) Delegated Regulation (EU) 2016/2251 provides for a phase-in over a number of years which reflects the implementation schedule agreed in the BCBS and IOSCO framework. That phase-in aims at ensuring international consistency and thus minimising possibilities of regulatory arbitrage. The phase-in also aims at facilitating a proportionate and effective implementation of the requirements by providing counterparties time to adapt their internal systems and processes to comply with the

[11] OJ L 201, 27.7.2012, p. 1.

[12] Commission Delegated Regulation (EU) 2016/2251 of 4 October 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty (OJ L 340, 15.12.2016, p. 9).

requirements depending on the category of counterparty to those contracts, on the type of contract and on when the contract was entered into or novated. Finally, the phase-in provided for in Delegated Regulation (EU) 2016/2251 takes into account the scope and level of implementation of the BCBS and IOSCO framework in other jurisdictions in order to avoid market fragmentation and ensure a global level playing field for counterparties established in the Union. In particular, Delegated Regulation (EU) 2016/2251 provides for more time for certain products that are not subject to equivalent margin requirements in other jurisdictions.

(3) The implementation schedule agreed in the BCBS and IOSCO framework has now been amended in the interest of supporting the smooth and orderly implementation of the margin requirements at the international level, in particular given the difficulties faced by smaller counterparties in meeting the originally envisaged deadline. In addition, there are still third countries in which certain products are not subject to equivalent margin requirements. In order to ensure a level playing field and market stability, by limiting the risk of regulatory arbitrage and facilitating a smooth implementation, the need to take into account the different level of progress made to date across jurisdictions and the changes in the implementation schedule agreed in the BCBS and IOSCO framework should be reflected in the phase-in provided for in Delegated Regulation (EU) 2016/2251 is necessary.

(4) Many counterparties enter into physically settled foreign exchange forward and physically settled foreign exchange swap contracts to hedge their risks associated with their currency risk exposures. In view of the specific risk profile of these contracts and the need for international regulatory convergence, it is appropriate to restrict the mandatory exchange of variation margin for these contracts between the most systemic counterparties, a permanent exemption should be introduced for these contracts when entered into with non-institutions.

(5) The European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority (the ESAs) have monitored the progress that has been made by counterparties to implement the initial margin requirements for non-centrally cleared derivatives and are aware that in the final phase of implementation, the initial margin requirements are scheduled to apply to a large number of entities for the first time. In the interest of supporting the smooth and orderly implementation of the margin requirements which is also consistent and harmonised across the member jurisdictions of the BCBS-IOSCO framework and helps avoid market fragmentation that could otherwise ensue, the deadline for the implementation of the initial margin requirements should be extended, with the introduction of an additional implementation phase whereby covered counterparties with an aggregate average notional amount of non-centrally cleared derivatives between €8 billion and €50 billion would have an extra year before becoming subject to the requirements, in line with the amended BCBS-IOSCO framework.

(6) Following the Covid-19 outbreak, the ESAs have monitored the impact on the financial markets of the rapid spread of the coronavirus disease, in particular with respect to the significant challenges posed to counterparties by Covid-19, including the displacement

of staff and the need to focus resources on managing risks associated with the related market volatility. In the interest of supporting the smooth and orderly implementation of the margin requirements which is also consistent and harmonised across the member jurisdictions of the BCBS-IOSCO framework and in order to provide additional operational capacity for counterparties to respond to the immediate impact of Covid-19, the deadline for the implementation of the initial margin requirements should be further extended. This extension would result in covered counterparties with an aggregate average notional amount of non-centrally cleared derivatives above €50 billion being subject to the requirements from 1 September 2021, and covered counterparties with an aggregate average notional amount of non-centrally cleared derivatives above €8 billion being subject to the requirements from 1 September 2022, in line with the BCBS-IOSCO framework, as further amended in response to the Covid-19 outbreak.

(7) Delegated Regulation (EU) 2016/2251 provides for a deferred date of application of the bilateral margin requirements for non-centrally cleared OTC derivative contracts concluded between counterparties which are part of the same group and where one counterparty is established in a third country and the other counterparty is established in the Union. That deferred date was necessary to ensure that such OTC derivative contracts were not subject to the bilateral margin requirements before the adoption of an implementing act pursuant to Article 13(2) of Regulation (EU) No 648/2012. To date, only two such implementing acts have been adopted. This situation is similar to the one with respect to the clearing obligation, which was first addressed in Commission Delegated Regulation (EU) 2019/667 [13]. The application of the bilateral margin requirements for non-centrally cleared OTC derivative intragroup contracts should therefore be further deferred until the adoption of such implementing acts, or, where no such implementing act is adopted until the 30 June 2022, keeping the same incentive as for the clearing obligation.

(8) To avoid market fragmentation and to ensure a global level playing field for counterparties established in the Union, international regulatory convergence should also be ensured with regard to risk-management procedures for other classes of OTC derivatives that are not subject to equivalent margin requirements. In particular, acknowledging the fact that in some jurisdictions single-stock equity options and index options are not subject to equivalent margin requirements, and that it is unlikely, especially in the current context, that these jurisdictions will move anytime soon towards more regulatory convergence with regard to those products, the treatment of those products should be further phased-in, i.e. until 4 January 2024. That further phase-in period should provide time for monitoring regulatory developments in other jurisdictions and should ensure that appropriate requirements are in place in the Union to mitigate counterparty credit risk in respect of such contracts whilst avoiding scope for regulatory arbitrage.

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[13] Commission Delegated Regulation (EU) 2019/667 of 19 December 2018 amending Delegated Regulations (EU) 2015/2205, (EU) 2016/592 and (EU) 2016/1178 to extend the dates of deferred application of the clearing obligation for certain OTC derivative contracts.

(9) On 29 March 2017, the United Kingdom of Great Britain and Northern Ireland (the 'United Kingdom') submitted the notification of its intention to withdraw from the Union pursuant to Article 50 of the Treaty on European Union. On 17 October 2019, the Union and the United Kingdom reached an agreement on the Withdrawal Agreement14, with a revised Protocol on Ireland and Northern Ireland and a revised Political Declaration15. Pursuant to that agreement and following its ratification by the House of Commons in the United Kingdom, its adoption by the European Parliament and its conclusion by the Council, the United Kingdom became a third country on 1 February 2020 and Union law will cease to apply to and in the United Kingdom on 31 December 2020.

(10) Commission Delegated Regulation (EU) 2019/397 ([2]) provided for an amendment to Delegated Regulation (EU) 2016/2251 ([3]) as regards the date until which counterparties may continue to apply their risk-management procedures for certain OTC derivative contracts not cleared by a CCP. Pursuant to Article 2 of Delegated Regulation (EU) 2019/397, that Regulation is to apply from the date following that on which the Treaties cease to apply to and in the United Kingdom pursuant to Article 50(3) of the Treaty on European Union, unless a withdrawal agreement has entered into force by that date or the two-year period referred to in Article 50(3) of the Treaty on European Union has been extended.

(11) By letter of 20 March 2019, the United Kingdom submitted a request for an extension of the period provided for in Article 50(3) of the Treaty on European Union until 30 June 2019, with a view to finalising the ratification of the Withdrawal Agreement ([4]). On 21 March 2019, the European Council agreed to an extension until 22 May 2019, provided the Withdrawal Agreement is approved by the House of Commons in the following week. If that is not the case, the European Council agreed to an extension until 12 April 2019. Consequently, Delegated Regulation (EU) 2019/397 did not apply.

(12) Commission Delegated Regulation (EU) 2019/564 ([5]) provides for an amendment to Delegated Regulation (EU) 2016/2251. Pursuant to Article 2 of Delegated Regulation (EU) 2019/564 that Regulation was to apply from the date following that on which the Treaties cease to apply to and in the United Kingdom pursuant to Article 50(3) of the Treaty on European Union, unless a withdrawal agreement had entered into force by that date or a decision had been taken to extend the two year period referred to in Article 50(3) of the Treaty on European Union beyond 31 December 2019.

(13) The application of Delegated Regulation (EU) 2019/564 was conditional on the absence of a withdrawal agreement, thus that Delegated Regulation did not apply. However, the reasons underlying Delegated Regulations (EU) 2019/397 and 2019/564 will remain relevant also following the expiry of the transition period. In particular, the risks to the smooth functioning of the market and a level playing field between counterparties established in the Union will persist in the case of the United Kingdom's withdrawal

[14] Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community (OJ C 384I, 12.11.2019, p. 1)
[15] Political declaration setting out the framework for the future relationship between the European Union and the United Kingdom (OJ C 384I, 12.11.2019, p. 178)

from the Union without an agreement establishing relationships with the European Union after the transition period, addressing the risks in question. Those risks are expected to remain for the foreseeable future.

(14) Delegated Regulation (EU) 2016/2251 should therefore be amended accordingly.

(15) This Regulation is based on the draft regulatory technical standards submitted by the ESAs to the Commission.

(16) The amendments to Delegated Regulation (EU) 2016/2251 are limited adjustments of the existing regulatory framework in line with international developments. Given the limited scope of the amendments and the urgency of the matter, it would be disproportionate for the ESAs to conduct open public consultations or analyses of the potential related costs and benefits. The ESAs nevertheless requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council[16], the opinion of the Insurance and Reinsurance Stakeholder Group and the Occupational Pensions Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1094/2010 of the European Parliament and of the Council[17], and the opinion of the Securities and Markets Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1095/2010 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council[18].

(17) It is necessary to provide market participants legal certainty as quickly as possible so that they can adequately prepare for complying with the requirements under EMIR the application of which will be affected by this Delegated Regulation, in particular with respect to the requirements for which the current applicable deadline is approaching rapidly. This Regulation should therefore enter into force as a matter of urgency.

HAS ADOPTED THIS REGULATION:

Article 1

Amendment to Delegated Regulation (EU) 2016/2251

Delegated Regulation (EU) 2016/2251 is amended as follows:

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[16] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

[17] Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

[18] Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

(1) the following Article 31a is inserted:

"*Article 31a*

Treatment of physically settled foreign exchange forwards and physically settled foreign exchange swaps

By way of derogation from Article 2(2), counterparties may provide in their risk management procedures that variation margins are not required to be posted or collected for physically settled foreign exchange forward contracts and physically settled foreign exchange swap contracts where:

one of the counterparties is not an institution as defined in point (3) of Article 4(1) of Regulation (EU) No 575/2013 or would not qualify as such an institution if it were established in the Union.";

(2) Article 35 of Delegated Regulation (EU) 2016/2251 is replaced by the following:

"Article 35

Transitional provisions

1. Counterparties referred to in Article 11(3) of Regulation (EU) No 648/2012 may continue to apply the risk-management procedures that they have in place at the date of application of this Regulation in respect of non-centrally cleared OTC derivative contracts entered into or novated between 16 August 2012 and the relevant dates of application of this Regulation.

2. Counterparties referred to in Article 11(3) of Regulation (EU) No 648/2012 may also continue to apply the risk-management procedures that they have in place on [OP: Please insert the date of entry into force of this Amending Regulation] in respect of non-centrally cleared OTC derivative contracts fulfilling all of the following conditions:

(a) the non-centrally cleared OTC derivative contracts have been entered into or novated before either the relevant dates of application of this Regulation as set out in Articles 36, 37 and 38 of this Regulation or [OP: Please insert the date of entry into force of this Amending Regulation], whichever is earlier;

(b) the non-centrally cleared OTC derivative contracts are novated for the sole purpose of replacing a counterparty established in the United Kingdom with a counterparty established in a Member State;

(c) the non-centrally cleared OTC derivative contracts are novated between 1 January 2021 and either of the following, whichever is later:

(i) the relevant dates of application set out in Articles 36, 37 and 38 of this Regulation; or

(ii) 1 January 2022.";

(3) Article 36 is amended as follows:

(a) paragraph 1 is amended as follows:

(i) point (e) is replaced by the following:

"(e) from 1 September 2021, where both counterparties have, or belong to groups each of which has, an aggregate average notional amount of non-centrally cleared derivatives that is above EUR 50 billion;";

(ii) the following point is added:

"(f) from 1 September 2022, where both counterparties have, or belong to groups each of which has, an aggregate average notional amount of non-centrally cleared derivatives that is above EUR 8 billion.";

(b) in paragraph 2, point (a) is replaced by the following:

"(a) from 30 June 2022 where no equivalence decision has been adopted pursuant to Article 13(2) of Regulation (EU) No 648/2012 for the purposes of Article 11(3) of that Regulation in respect of the relevant third country;";

(4) in Article 37(3), point (a) is replaced by the following:

"(a) from 30 June 2022 where no equivalence decision has been adopted pursuant to Article 13(2) of Regulation (EU) No 648/2012 for the purposes of Article 11(3) of that Regulation in respect of the relevant third country;";

(5) in Article 38, paragraph 1 is replaced by the following:

"1. By way of derogation from Articles 36(1) and 37, in respect of all non-centrally cleared OTC derivatives which are single-stock equity options or index options, the Articles referred to in Articles 36(1) and 37 shall apply from 4 January 2024."

Article 2
Entry into force

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

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission
The President

[For the Commission
On behalf of the President

[Position]

3.3 Annex III – Feedback from the consultation of the Stakeholder Groups as to amendments to the bilateral margin requirements in view of the international framework

76. As mentioned at the start of this Report, the stakeholder groups of each of the ESAs have been consulted on amendments related to the provisions covered in the draft RTS.

77. While no formal position of each of the 4 relevant Stakeholder Groups of the ESAs could be established in the time provided, a few subject matter experts from these groups with respect to the topic covered, bilateral margining of uncleared OTC derivatives, answered and provided feedback on the proposed amendments.

78. The feedback was overall positive, expressing full support to introduce such amendments. One respondent explained that "it addresses the outstanding concerns in terms of alignment with developments in the international framework for margining of non-cleared derivatives: timing and implementation of the final phases for smaller users, targeted exemptions for physically-settled fx forwards and fx swaps for non-systemic entities, and targeted exemptions for intragroup transactions and certain equity options."

79. There was not a single contribution objecting against the introduction of such amendments.

80. However, the respondents also added that the initially proposed one-year extension of the exemption for single-stock equity options and index options was too short and advocated for a two-year extension instead, possibly with a review clause.

81. First of all, the concern raised is that a one-year extension does not provide market participants with an adequate timeframe in terms of visibility and planning. Secondly, and more fundamentally, they argue that the situation of unlevel playing field has not changed and is unlikely to change at least in the next 6 months, and as a result that this issue will need to be addressed again very shortly.

82. The ESAs take note of both the full support to introduce such amendments quickly as well as with regards to the concerns raised on the length of the extension of the exemption for single-stock equity options and index options. First of all, the overall support reinforces the need to proceed rapidly and submit the draft RTS to the Commission. Secondly, with regards to the length of the extension of the exemption, the ESAs reiterate the importance of the global framework and ensuring international convergence, the length for the single-stock equity options and index options exemption has been considered further in the last version of the draft RTS taking into account the overall context this year.