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ECON-Draft Report: Assessment

Retain fundamental EMIR-principles like the hedging exemption

Proposal for a Regulation amending Regulations (EU) No 648/2012, (EU) No 575/2013 and (EU) 2017/1131 (EMIR 3.0), Committee on Economic and Monetary Affairs, draft report by Danuta Hübner, 21 August 2023

The exemption for hedging derivatives is vital for the real economy

Deutsches Aktieninstitut follows the EMIR legislation very closely, expressing the view of non-financial companies using derivatives in their risk management. We commented on the Commission's proposal for a regulation amending EMIR. Our main concern was the proposed removal of the exemption of **the reporting requirements for intra-group transactions** and the changes of Article 10 (3), that **would no longer allow for centralised risk management of corporates** under certain circumstances.

In this regard, we very much welcome amendments which re-introduce the exemption for intra-group transactions (amendments 10, 50, 221, 222) and the possibility to hedge on group level (amendments 56 and in principle 304). **Nevertheless, we strictly oppose amendments intended to fundamentally change the EMIR regime regarding non-financial companies, especially the removal of the hedging definition (amendments 305, 306, 307 and 308).** That definition is a central cornerstone of EMIR's practical feasibility for the real economy, and a prerequisite for the adequacy of this regulation in general. In the end, this would mean that companies with larger derivative exposures fall under the clearing obligation, although they mainly/exclusively use derivatives to mitigate risks from fluctuations of currencies, interest rates or commodity prices.

Besides the helpful amendments mentioned above, we further support…

- …amendments 58 and 59 which maintain the Commission's proposal to grant non-financial firms exceeding a clearing threshold (so-called "NFC+") for the first time a 4-months phase-in of their mark-to-market and bilateral margining obligations. Furthermore, amendment 59 limits the bilateral margining obligation to the asset class(es) for which the clearing threshold has been exceeded. This is aligned with the same "asset class approach" taken with regards to the clearing obligation (Art. 11);

- …amendments 163, 164, 465 and 468 confirm that non-financial firms, in particular energy market participants, can continue to act as direct clearing members (Art. 37);

- …amendments 22, 165, 166, 469, 470 and 471 as they further improve the transparency and predictability of margin calls (Art. 38);

- …amendments 170, 172, 469, 470 and 471 as they maintain the EC's proposal and explicitly clarify that uncollateralized commercial bank guarantees can be used as eligible collateral (Art. 46).

Nevertheless, we reject the following amendments:

- Amendments 305, 306, 307 and 308 refer to Art. 10 and the exemption of risk-mitigating derivatives, which are of no relevance for the calculation of the clearing thresholds. We strongly oppose these amendments, as companies with larger derivative exposure would cross the clearing thresholds, becoming obliged to clear/to put aside margins billaterally, although they use derivatives mainly/exclusively to hedge their operative business. These amendments fundamentally contradict the generally agreed upon principle that risk-mitigating derivatives used are of strategic importance in the risk management of non-financial companies. Hedging with derivatives stabilizes cash flows thus enhancing creditworthiness and long-term ratings of NFCs. As such, risk-mitigating derivatives do not contribute to systemic risks in the financial system.

- We oppose amendment 310 which introduces risk mitigation techniques for non-financial companies not clearing obliged “equivalent to those of a CCP”. It is completely unjustified to require the same strict risk mitigating techniques common for CCP clearing. In the extreme, this could mean mandatory margining (collateralization), which would contradict the exemption from this requirement and the general acknowledged aim of legislator/regulator, to treat especially hedging derivatives from non-financial companies different (see the bullet above). Again, these transactions do not contribute to systemic risks in financial markets.

- Amendments 203, 249 and 250 delete the Commission’s proposal to exempt cleared OTC-derivatives from the clearing threshold calculation. This amendment ist not justified at all, as clearing already mitigates the risk of these instruments, even if they are not used for hedging purposes. To note, these transactions are to be reported under EMIR further and transparency is ensured.

- Amendment 49 extends the reporting obligation to non-EU entities on a general basis, even if no EU-product, EU-venue or EU-entity is involved. This extension would impose unnecessary and disproportionate reporting requirements by subjecting non-EU entities to the EMIR reporting obligation in addition to third country reporting obligations such as UK EMIR (for UK entities) or Dodd-Frank (for US entities). This proposal negates the principles of substituted equivalence and regulatory cooperation which have been put at the core of financial market regulation following the 2008 financial crisis. Such an initiative will put European non-financial groups at a competitive disadvantage as they will face double reporting obligations and associated costs which might only be increased by non-EU regulators taking a similar stance. In addition, we

do not see any additional benefit from a supervisory perspective by this double reporting. For these reasons we urge to delete amendment 49.

- We oppose amendment 296 which reintroduces equivalence as a precondition for NFCs- to be exempt from reporting requirements on transactions with third country entities. We also oppose amendment 223, which proposes additional reporting preconditions for non-financial companies.

- We support the EC proposal in relation to the clearing threshold calculations for non-financial firms on entity level as it safeguards European competitiveness. Extending the clearing threshold calculation to include global turnover, as proposed by amendments 55, 56, 305 and 306 will have opposite adverse effects. Therefore, we urge to maintain the Commission's proposal to count exclusively the OTC derivative transactions entered into by EU established counterparties against the clearing thresholds and do not support amendments 55 and 56.

- So far, clearing thresholds in Art. 10(1) EMIR are calculated as the "aggregate month-end average position for the previous 12 months". Amendments 248, 299, 300 aim to replace this calculation method by the "average of the three highest month-end averages positions over the previous 12 months". We reject these amendments as they might force companies into the clearing obligation although they solely crossed the clearing thresholds for a short time period.

- We are concerned about the unclear wording and purpose of amendment 57, which in its current form applies exclusively to financial counterparties. This amendment provides that ESMA shall assess whether an aggregate activity threshold is necessary, taking into account the overall aggregate position in OTC derivatives of a financial counterparty. The undetermined purpose provides an open mandate to ESMA and creates legal uncertainly as to the motives pursued. We disagree with this proposal if its purpose would be to prohibit financial counterparties (and non-financial counterparties) to fully use the clearing thresholds in the different relevant asset classes. The new calculation methodology of cleared versus non-cleared derivatives does not request a change to this asset class approach as the purpose of these thresholds remains unchanged, i.e., to mitigate the credit risks of non-cleared (OTC) derivatives.

- We oppose amendments 199, 200 and 246 as they keep the Art. 13 equivalence decision as a pre-condition to availability of the exemption from the requirement, that intra-group transactions with third country subsidiaries have to be collateralised bilaterally. We also object

amendments 201 and 247 that extend the list of non-cooperative tax jurisdictions to those on the grey list.

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