



European Securities and  
Markets Authority

# Report

**MIFID II: C6 energy derivative contracts and the EMIR requirements**



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# 1 Executive Summary

## Reasons for publication

ESMA has developed this report on C6 energy derivative contracts in relation to some of the EMIR<sup>1</sup> obligations as an input to the European Commission's own report on this same topic that is mandated under Article 90(4) of MiFID. In particular, the report has to look into the impact, cost, adequacy and feasibility of C6 energy derivative contracts being made subject to:

- the clearing obligation set out in Article 4 of EMIR
- the risk mitigation techniques set out in Article 11(3); and
- their inclusion in calculating the clearing threshold pursuant to Article 10.

Following from this analysis, this report would thus help decide whether a legislative change is required and whether some of the transitional measures should be extended.

## Contents

The report is divided into 7 Sections:

Section 2 focuses on the scope of the report;

Section 3 introduces generally the issue investigated in the report;

Section 4 focuses in the C6 energy derivative contracts and it is divided into two parts: (i) the regulatory framework and the temporary exemption from certain EMIR requirements, and (ii) the use of C6 energy derivative contracts;

Section 5 analyses the potential impact of the EMIR requirements on C6 energy derivative contracts and in particular, (i) impact regarding the clearing obligation; (ii) impact regarding the requirement to exchange collateral; and (iii) impact of including C6 energy derivative contracts in the calculation of positions against the clearing thresholds;

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<sup>1</sup> Regulation (EU) No 648/2012.

Section 6 regards the conclusions of the report; and

Section 7 includes ESMA's recommendations.

### **Next Steps**

This report has been submitted to the European Commission before its publication on the ESMA website, as input for the European Commission's report under Article 90(4) of MiFID.

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## 2 Scope of the Report

1. This report focuses on the adequacy of mandating C6 energy derivative contracts to be subject to certain EMIR obligations for which they currently benefit from a temporary exemption. In particular, this report refers to the following EMIR requirements:
  - a. The clearing obligation;
  - b. The exchange of collateral; and
  - c. The inclusion of such contracts in the calculation for the purpose of determining counterparties' positions against the clearing thresholds.
2. ESMA investigates in this Report on the one hand, the uses of such contracts by non-financial counterparties (NFCs), and on the other hand, the potential benefits in terms of reducing counterparty and systemic risks and the impact of C6 energy derivative contract made subject to the above-mentioned EMIR requirements.

## 3 Introduction

3. To start with, C6 energy derivative contracts refer to derivative contracts relating to coal or oil that are traded on an OTF and that are physically settled (see section 4.1 for a more detailed analysis).
4. MIFID II<sup>2</sup> provides for a transitional regime for C6 energy derivative contracts, which until 3 January 2021 are temporarily exempted from the clearing obligation and from the requirement to exchange collateral for contracts entered into by non-financial counterparties that are above the clearing threshold (NFC+) or by investment firms authorised for the first time as of 3 January 2018.
5. In addition, this temporary regime also excludes C6 energy derivative contracts from the calculation for the purpose of the clearing thresholds. Therefore, C6 energy derivative contracts do not have an impact when determining whether an NFC is subject to the clearing obligation.
6. The Commission, after consulting ESMA and ACER, has to prepare a report on whether certain EMIR obligations should apply to C6 energy derivative contracts; in particular, assessing the potential impact on energy prices and on the functioning of the energy market as well as the feasibility and the benefits in terms of reducing counterparty and systemic risks and the direct costs of C6 energy derivative contracts being made subject to the clearing obligation, the risk mitigation techniques set out in Article 11(3) and their inclusion in calculating the clearing threshold pursuant to Article 10 (which refers to NFCs).

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<sup>2</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065&from=EN>

## 4 C6 energy derivative contracts

### 4.1 Regulatory framework and the temporary exemption from EMIR requirements

7. The current regulatory framework for C6 energy derivative contracts in relation to the considerations in scope for this report is set in both EMIR and MiFID.
8. To begin with, the definition of derivative contracts under EMIR, which will define the scope of contracts subject to the EMIR requirements such as the clearing obligation and the requirement to exchange collateral, cross refers to MiFID:

‘Derivative contract’ means a financial instrument as set out in points (4) to (10) of Section C in Annex I of MIFID II.

9. In MiFID, there is thus the list of instruments that are considered financial instruments. Section C in Annex I of MIFID II lists from (1) to (11) the different financial instruments and, within that list, EMIR refers to financial instruments under numbers (4) to (10) as derivative contracts.

10. Notably, Section C 6 of this Annex refers to:

‘Options, futures, swaps, and any other derivative contract relating to commodities that can be physically settled provided that they are traded on a regulated market, a MTF, or an OTF, except for wholesale energy products traded on an OTF that must be physically settled;’

11. ESMA clarified the way in which this provision is interpreted in ESMA’s Technical Advice to the Commission on MiFID II and MiFIR in 2014<sup>3 4</sup>:

*“Section C 6 of Annex I excludes wholesale energy products within the scope of REMIT that are traded on an OTF and that must be physically settled. Therefore, these excluded wholesale energy products do not qualify as financial instruments and are consequently outside the scope of MiFID, EMIR and the CRD IV package. Wholesale energy products within the scope of REMIT which are derivatives contracts, and therefore are within the scope of this exemption, are derivatives with electricity (or power) or natural gas as the underlying.”<sup>5</sup>*

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<sup>3</sup> ESMA’s technical advice to the Commission on MIFID II and MiFIR:  
[https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1569\\_final\\_report\\_-\\_esmas\\_technical\\_advice\\_to\\_the\\_commission\\_on\\_mifid\\_ii\\_and\\_mifir.pdf](https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1569_final_report_-_esmas_technical_advice_to_the_commission_on_mifid_ii_and_mifir.pdf)

<sup>4</sup> In 2015, ESMA also issued guidelines on the application of the definitions in Sections C6 and C7 of Annex I of MiFID:  
[https://www.esma.europa.eu/sites/default/files/library/2015/11/2015-05-06\\_final\\_guidelines\\_c6\\_and\\_7.pdf](https://www.esma.europa.eu/sites/default/files/library/2015/11/2015-05-06_final_guidelines_c6_and_7.pdf)

<sup>5</sup> ESMA’s technical advice to the Commission on MIFID II and MiFIR (2014):  
[https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1569\\_final\\_report\\_-\\_esmas\\_technical\\_advice\\_to\\_the\\_commission\\_on\\_mifid\\_ii\\_and\\_mifir.pdf](https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1569_final_report_-_esmas_technical_advice_to_the_commission_on_mifid_ii_and_mifir.pdf)

12. In addition, Article 4(16) of MIFID II provides a definition of C6 energy derivative contracts that narrows it down to coal or oil related products:

‘C6 energy derivative contracts’ means options, futures, swaps, and any other derivative contracts mentioned in Section C 6 of Annex I relating to coal or oil that are traded on an OTF and must be physically settled;<sup>6</sup>

13. Certain aspects of EMIR apply generally to all types of derivative contracts, such as the reporting requirements under Article 9; while some other EMIR requirements can only apply when the derivative contracts qualify as OTC derivatives and when certain conditions are met.

14. As defined under EMIR, ‘*OTC derivative contracts*’ are those the execution of which does not take place on a regulated market<sup>7</sup> or a third country market considered to be equivalent to a regulated market<sup>8</sup>. As per the EMIR Q&A OTC Question 1<sup>9</sup>, derivatives traded on an OTF are OTC derivative contracts for the purpose of EMIR and thus subject to the relevant EMIR provisions under Article 4 and 11(3), i.e. the clearing obligation and the requirement to exchange collateral respectively; unless an exemption is provided.

15. MIFID II, in its transitional provision under Article 95, provides for a temporary exemption regime for certain counterparties trading with C6 energy derivatives contracts:

“1. *Until 3 January 2021:*

- a. the clearing obligation set out in Article 4 of Regulation (EU) No 648/2012 and the risk mitigation techniques set out in Article 11(3) thereof shall not apply to C6 energy derivative contracts entered into by non-financial counterparties that meet the conditions in Article 10(1) of Regulation (EU) No 648/2012 or by non-financial counterparties that shall be authorised for the first time as investment firms<sup>10</sup> as from 3 January 2018; and

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<sup>6</sup> The Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU refers to ‘Energy derivative contracts relating to oil and coal and wholesale energy products’ in Article 6.

<sup>7</sup> ‘regulated market’ means a multilateral system operated and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments – in the system and in accordance with its non-discretionary rules – in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with Title III of this Directive. Definition under Article 4(21) of MIFID II.

<sup>8</sup> Under Article 2a of EMIR, the European Commission may adopt an implementing act to determine the equivalence of a third country market to a EU regulated market for the purpose of EMIR. The list of third countries considered equivalent is available on ESMA’s website: [https://www.esma.europa.eu/sites/default/files/library/equivalent\\_tc-markets\\_under\\_emir.pdf](https://www.esma.europa.eu/sites/default/files/library/equivalent_tc-markets_under_emir.pdf)

<sup>9</sup> The Questions and Answers on the implementation of EMIR can be found on ESMA’s website:

[https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52\\_qa\\_on\\_emir\\_implementation.pdf](https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf)

<sup>10</sup> Article 2 in MIFID II exempts persons dealing on own account, or providing investment services to clients, in commodity derivatives, emission allowances or derivatives thereof, provided this is an ancillary activity to their main business on a group basis and the main business is not the provision of investment services within the meaning of MiFID II or banking activities under Directive 2013/36/EU. The Commission Delegated Regulation (EU) 2017/592 further specifies the criteria to establish when an activity is considered to be ancillary to the main business and provides different thresholds for different asset classes to test whether the persons within the group are large participants relative to the size of the financial market in that asset class (test 1); and whether the persons within the group trade on own account or provide investment services in commodity derivatives, emission allowances or derivatives to an extent that cannot be considered to be ancillary (test 2). These two tests

- b. such C6 energy derivative contracts shall not be considered to be OTC derivative contracts for the purposes of the clearing threshold set out in Article 10 of Regulation (EU) No 648/2012.

*C6 energy derivative contracts benefiting from the transitional regime set out in the first subparagraph shall be subject to all other requirements laid down in Regulation (EU) No 648/2012.*

*2. The exemption referred to in paragraph 1 shall be granted by the relevant competent authority. The competent authority shall notify ESMA of the C6 energy derivative contracts which have been granted an exemption in accordance with paragraph 1 and ESMA shall publish on its website a list of those C6 energy derivative contracts.”*

16. In practice, only NFCs are benefiting from this exemption because it would appear that to date none of the NFCs using derivatives as part of their activity have exceeded the thresholds that determine whether an NFC should seek authorisation as an investment firm (considered a financial counterparty under EMIR). Indeed, to ESMA's knowledge, no NFC using derivatives as part of their activity needed to obtain an authorisation as an investment firm<sup>11</sup>. For that reason, this Report mainly focuses on the impact of the MIFID II temporary exemption un Article 95 for NFCs.
17. Furthermore, it should be noted that ESMA has never received any notification under Article 95 of MiFID, and is thus not aware of any entity benefiting from the exemption provided for these products. This would thus imply there is not really any impact at this stage of this exemption. Nevertheless, given this situation could change, this report is still analysing the possible impact if some of the energy derivatives were in this category in the future.
18. In addition, although this is not strictly in the scope of this report, but for completeness, it is worth mentioning that ESMA has recently issued a consultation paper on the MiFID II review report on commodity derivatives<sup>12</sup>. One of the issues raised in the consultation paper relates to whether wholesale energy contracts in Annex I Section C (6) that are traded on an OTF and physically settled should continue to be exempted from MiFID II provisions, including from position limits and position reporting requirements. However, as previously clarified these C6 carved-out contracts only refer to wholesale energy products within the scope of REMIT i.e. derivatives with electricity (or power) or natural gas as the underlying<sup>13</sup>. Therefore, the conclusions of this report should not interfere in any manner with the findings of the consultation paper and subsequent final report on MIFID Review, as the present report focuses on derivative contracts (with specific characteristics) on coal or oil and the consultation paper, on electricity and natural gas.

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determine whether those activities cannot be considered ancillary and therefore the counterparty needs to obtain authorisation as an investment firm.

To ESMA's knowledge, no counterparty had to obtain authorisation as a result of these tests.

<sup>11</sup> See footnote 8.

<sup>12</sup> MiFID II review report on position limits and position management, available on ESMA's website:

<https://www.esma.europa.eu/press-news/esma-news/mifid-ii-esma-consults-position-limits-in-commodity-derivatives>

<sup>13</sup> See paragraph 7(b).

19. Going back to the current report assessing the benefits, impact and cost of making C6 energy derivative contracts subject to EMIR provisions after the end of the transitional period, it should be noted that under MiFID the Commission is empowered to adopt delegated acts extending this temporary regime for these contracts once by two years and a further time by one year.

## 4.2 The use of C6 energy derivative contracts

20. C6 energy derivative contracts are part of a broader asset class of derivatives, the commodity derivatives, and the second ESMA Statistical Report on EU derivatives Markets (2019)<sup>14</sup> provides a number of metrics on the related size and structure of this market.

21. In particular, the report displays the relative size and share of the commodity derivative market, which is thus much smaller in relative terms compared to the overall derivative market:

Table 1: Size of derivative asset classes by notional amount<sup>15</sup>.

Size	Derivatives asset class					
	All	Commodities	Credit	Currency	Equity	Interest rate
Total notional amount (EUR tn)	735	11	13	110	44	557
Proportion (% of total notional)	100	1	2	15	6	76
Change 1Q18 to 4Q18 (%)	5	-28	-11	-24	21	16
Contracts (number in mn)	66	9	1	32	17	8
Change 1Q18 to 4Q18 (%)	-33	-41	4	12	-60	-14
Proportion (% of total number)	100	13	1	49	25	12

22. The report also shows that a significant portion of the commodity derivatives executed in the EU are entered into by non-financial counterparties. Figure 1 below presents the proportion of total notional amount outstanding for commodity derivatives by types of counterparties in the last quarter of 2018.

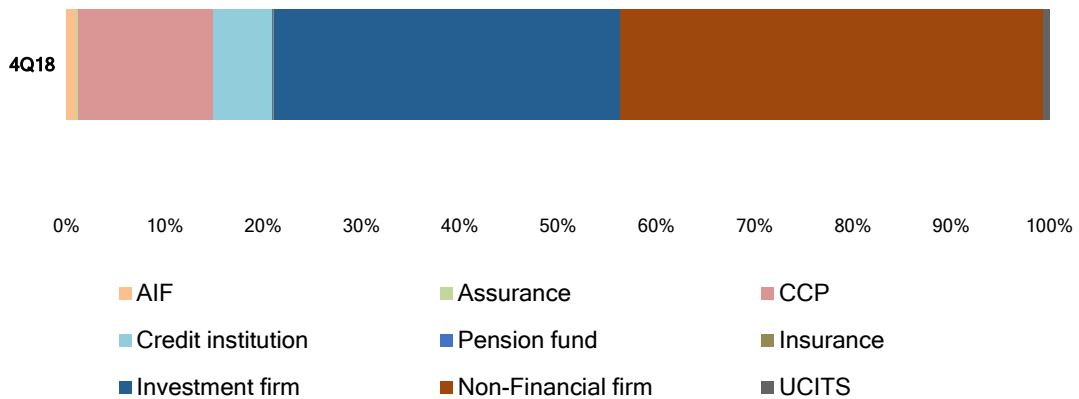
<sup>14</sup> The full report can be found here:

[https://www.esma.europa.eu/sites/default/files/library/esma50\\_157\\_2025\\_asr\\_derivatives.pdf](https://www.esma.europa.eu/sites/default/files/library/esma50_157_2025_asr_derivatives.pdf)

<sup>15</sup> This table is extracted from the ESMA annual Statistical Report on EU derivatives Markets (2019).



23. Figure 1: notional amount by sector of counterparty<sup>16</sup>.



Note: Proportions of total notional amount outstanding (not reconciled) by counterparty, in %.  
Sources: TRs, ESMA.

24. As it is shown, more than 55% of the notional amount outstanding is concentrated in non-financial counterparties in the last quarter of 2018. Similarly, when looking into the different counterparties' exposures per class of derivatives, the ESMA Report shows that non-financial firms account for 7% of the overall notional amount and that 41% of that notional amount is traded in commodities derivatives.

25. In addition, as part of the EMIR Review, ESMA published in August 2015, the EMIR Review Report no.1<sup>17</sup> which focused on the use of OTC derivatives by non-financial counterparties. It is apparent from that Report that NFCs use OTC derivative contracts, inter alia, mainly to cover themselves against risks directly linked to their commercial or treasury financing activities (hedging transactions).

26. The co-legislators appear to have taken this into account and therefore, EMIR was drafted with requirements applicable to NFCs that differ depending on the level of non-hedging activity of the NFC in OTC derivatives. Notably, when calculating positions against the clearing thresholds, which then determines the set of requirements that apply, NFCs do not consider trades that are entered into for hedging purposes, the so-called hedging exemption.

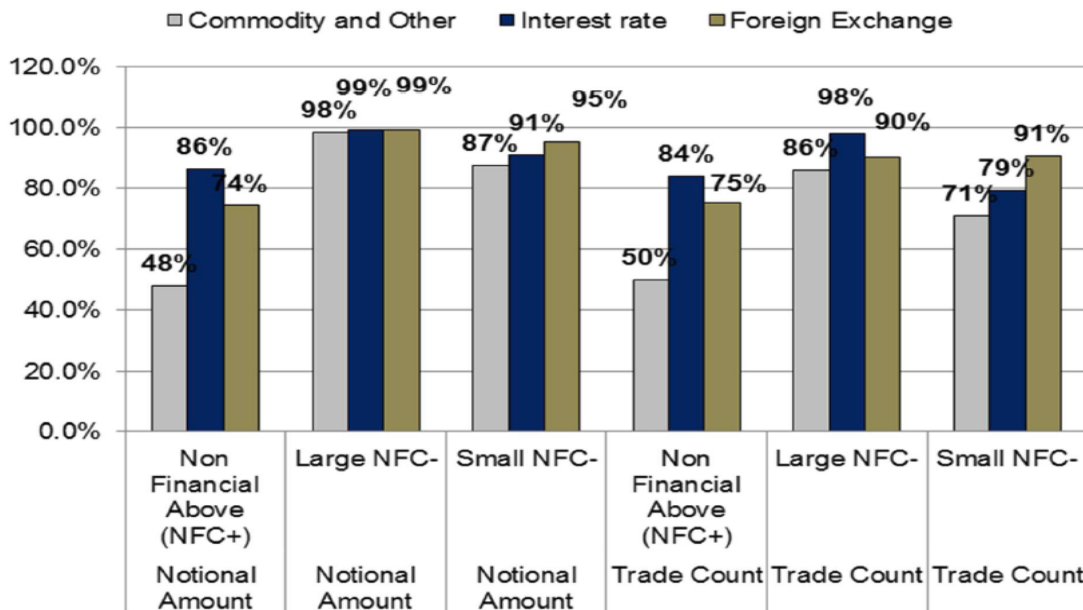
27. Figure 2 presents the share of hedging volumes reported by NFCs split into different classes of derivatives and between NFCs above the clearing threshold and NFCs below (distinguishing between large and small NFCs<sup>18</sup>), which in all cases is a relatively large share of the trades.

<sup>16</sup> Information extracted from the ESMA annual statistical Report on derivatives. The report can be found on ESMA's website: [https://www.esma.europa.eu/sites/default/files/library/esma50\\_157\\_2025\\_asr\\_derivatives.pdf](https://www.esma.europa.eu/sites/default/files/library/esma50_157_2025_asr_derivatives.pdf)

<sup>17</sup> The full report can be found on ESMA's website: <https://www.esma.europa.eu/sites/default/files/library/2015/11/esma-2015-1251-emir-review-report-no.1-on-non-financial-firms.pdf>

<sup>18</sup> According to the report's classification, the large NFCs represent less than 1% of the total NFCs.

28. Figure 2: Share of hedging volumes reported by NFCs<sup>19</sup>.



29. The EMIR Review Report investigated the proportion of OTC derivative contracts entered into for hedging purposes and concluded that across classes of derivatives, the proportion of the volumes traded for hedging purposes is around 73% (by notional amounts) for NFCs+; and even higher, around 96% (in notional amounts) for NFCs-.

30. Concerning the commodity asset class, while for NFCs- the proportion of the volumes traded for hedging purposes is around 92%, for NFCs+ it is much lower, around 48%. These figures show that a clear majority of commodity trades (in which C6 energy derivative contracts are included) are entered into by NFCs for hedging purposes. Therefore, because of the hedging exemption for NFCs, a large proportion of C6 energy derivative contracts would not count for the purpose of calculating positions against the clearing thresholds even if they were to be included in the calculation. This argument is further developed in Section 5.3.

## 5 Potential impact of EMIR requirements on C6 energy derivative contracts

### 5.1 Impact regarding the clearing obligation

31. With the overarching objective of reducing systemic risk, the European Market Infrastructure Regulation (“EMIR”) introduces the obligation to clear certain classes of OTC derivatives in Central Counterparties (CCPs) that have been authorised (for European CCPs) or recognised (for Third-country CCPs) under the EMIR framework.

<sup>19</sup> The source of this chart is the EMIR Review Report no 1.

Ensuring that the clearing obligation reduces systemic risk requires a process of identification of classes of derivatives that should be subject to mandatory clearing.

32. Currently, the clearing obligation is limited to two asset classes of OTC derivatives subject to the clearing obligation:
  - a. Interest rates OTC derivatives; and
  - b. Credit OTC derivatives.
33. Bearing in mind that only these two asset classes of OTC derivatives are mandated to be cleared, making C6 derivative contracts subject to EMIR requirements would not have an immediate impact on the clearing obligation as commodity derivatives are not currently subject to the clearing obligation.
34. EMIR foresees two possible processes for the identification of the relevant classes of OTC derivatives that could be used in the future to subject C6 energy derivative contracts to the clearing obligation:
  - a. The “bottom-up” approach described in EMIR Article 5(2), according to which the determination of the classes to be subject to the CO will be done based on the classes which are already cleared by authorised or recognised CCPs<sup>20</sup>; and
  - b. The “top-down” approach described in EMIR Article 5(3), according to which ESMA will on its own initiative identify classes which should be subject to the clearing obligation but for which no CCP has yet received authorisation.
35. Without prejudice to the possibility for ESMA to run one of the above two procedures to see whether new classes would be fit to be added to the scope of the clearing obligation, in view of the previous ESMA analysis and public consultations on the clearing obligation and in view of the relative size, structure and use of the C6 energy derivatives, C6 energy derivative classes would appear to be a of much lesser priority for the clearing obligation than other classes from other asset classes, for which ESMA did not at this stage mandate clearing.
36. In addition, it is important to note that EMIR Refit has changed the clearing requirements for the NFCs that are NFCs+, i.e. they only need to clear the mandated classes in the asset class where they exceed the clearing thresholds (this is further developed in Section 5.3). Hence, to complement the above, NFCs would need both to exceed the clearing thresholds in the commodity derivative asset class (for contracts not falling under the hedging exemptions) and for classes of C6 energy derivatives to

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<sup>20</sup> The Public Register lists all the CCPs authorised (and their extensions of authorisations in the case they extended their scope) or recognised that clear OTC derivatives. The “Public Register for the Clearing Obligation under EMIR” is available under the post-trading section of : <http://www.esma.europa.eu/page/Registries-and-Databases>

be in the scope of the clearing obligation, to be required to clear these classes if the exemption were to stop.

37. Furthermore, without entering into the details of the Brexit implications, it should be noted that an important share of commodity derivatives, and C6 energy derivatives more specifically given the scope of this report, are cleared in the United Kingdom. And in view of the Brexit developments, there is some uncertainty on how the regulatory framework applying in the case of these C6 energy derivative contracts may evolve, which would one reason to follow a prudent approach here for the moment.

## 5.2 Impact regarding the requirement to exchange collateral

38. Under EMIR, counterparties have an obligation to protect themselves against credit exposures to derivatives counterparties by collecting margins where those contracts are not cleared by a central counterparty, although different levels of requirements may apply based on the nature of the counterparty and the size of their OTC derivative activity. This requirement stems from the international standards designed by the BCBS and IOSCO for the exchange of bilateral margin along with a calendar to facilitate a consistent implementation across jurisdictions. In the European Union, such framework was further specified in Commission Delegated Regulation (EU) No 2016/2251 on bilateral margining<sup>21</sup>.

39. 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. For instance, counterparties with smaller portfolios and generally smaller operations are allowed more time before having to comply with the initial and variation margin requirements and counterparties below the 8 Billion threshold are not subject to the initial margin requirements.

40. Collecting margins for non-cleared OTC derivative transactions is hence a protection for counterparties against the fluctuation in value of outstanding contracts and the risk of default of the counterparty and requires a liquidity effort from counterparties that should be proportional to their size and trading strategy. Margin requirements distinguish between variation margin<sup>22</sup> and initial margin<sup>23</sup> and each requirement has a phase-in calendar of implementation.

41. Regarding the variation margin requirement, counterparties had to comply depending on the aggregate average notional amount of non-cleared OTC derivatives of their group's; and at the latest, by 1 March 2017. Therefore, counterparties trading with C6

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<sup>21</sup> The ESAs under Article 11(15) of EMIR have a joint mandate under which they developed the Regulatory Technical Standards on bilateral margin.

<sup>22</sup> According to The Commission Delegated Regulation (EU) 2016/2251, 'variation margin' means the collateral collected by a counterparty to reflect the results of the daily marking-to-market or marking-to-model of outstanding contracts referred to in Article 11(2) of Regulation (EU) No 648/2012.

<sup>23</sup> According to The Commission Delegated Regulation (EU) 2016/2251, 'initial margin' means the collateral collected by a counterparty to cover its current and potential future exposure in the interval between the last collection of margin and the liquidation of positions or hedging of market risk following a default of the other counterparty.

energy derivatives contracts, if such contracts were to become subject to margin rules, would immediately have to post variation margin.

42. Initial margin requirements are still in the phase-in process and counterparties are divided into categories (up to five) depending on the aggregate average notional amount of non-cleared OTC derivatives in their groups. Counterparties in Category 5, belonging to groups with a smaller aggregate average notional amount (more than €8 billion), will only become subject by 1 September 2020.
43. However, the ESAs have supported through a Final Report<sup>24</sup> recently published an amendment advocated by the BCBS and IOSCO to:
  - a. create an additional intermediate category of counterparties (between current category 4 and category 5) for counterparties which group's aggregate average notional amount of non-cleared OTC derivatives is above €50 billion. For this modified category 5, initial margin requirements would start applying on 1 September 2020; and to
  - b. delay the deadline for the initial margin requirements for counterparties belonging to groups with an aggregate average notional amount of more than €8 billion (and below €50 billion, the newly proposed category 6) to 1 September 2021.
44. Therefore, taking both the initial margin phase-in and the current C6 energy derivative temporary exemption into account, the margin requirements have not had much of an impact on that market yet. However, if the temporary exemption were to stop, in the context of understanding the impact on C6 energy derivatives, it is important to remember that the requirement of Article 11(3) of EMIR only applies to NFCs+, which are the NFCs above the clearing thresholds, which is discussed in the next section.

### **5.3 Impact of including C6 energy derivative contracts in the calculation of positions against the clearing thresholds**

45. EMIR, as amended by Refit, has now a modified mechanism to determine which counterparties are subject to the clearing obligation and for which classes of derivatives.
46. For NFCs, first of all, Refit maintains the use of the clearing thresholds<sup>25</sup>, i.e. that under EMIR Refit, NFCs may calculate their positions against the clearing thresholds to know whether they are NFCs+. However, the new Refit regime also introduces a particularity regarding the calculation; counterparties can now choose whether to calculate their positions against the clearing thresholds or choose not to calculate them, in which case,

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<sup>24</sup> ESAs Final Report on EMIR RTS on various amendments to the bilateral margin requirements in view of the international framework: [https://www.esma.europa.eu/sites/default/files/library/esas\\_2019\\_20\\_-\\_final\\_report\\_-\\_bilateral\\_margin\\_amendments.pdf](https://www.esma.europa.eu/sites/default/files/library/esas_2019_20_-_final_report_-_bilateral_margin_amendments.pdf)

<sup>25</sup> The clearing thresholds have been defined by asset class and set under Article 11 of Commission Delegated Regulation (EU) No 149/2013.



they will be considered subject to the clearing obligation for all classes mandated to be cleared.

47. Secondly, Refit changes the obligation for NFCs+, narrowing the scope of the clearing obligation to only apply in the asset class or classes for which the NFC has effectively exceeded the clearing thresholds.
48. Lastly, with regards to the question on how to calculate its positions to determine whether the clearing thresholds are exceeded, the scope of contracts included in the calculation for NFCs has not been amended (NFCs only need to include OTC contracts entered into by the NFC or by the other NFCs within its group and excluding hedging transactions<sup>26</sup>), but the calculation has changed, from a rolling average over 30 days to the aggregate month-end average position for the previous 12 months.
49. One key finding since the EMIR Review Report No.1 on the activity of NFCs, was that the population of NFCs+ is limited due to the hedging exemption in the calculation. Indeed, ESMA data shows that around 90% of trades in commodity derivatives entered into by NFCs are to hedge their risks, it is thus expected that the inclusion of C6 energy derivative contracts in the calculation of positions would not have a major impact on NFCs for the purpose of the clearing thresholds and the related requirements.
50. However, similar to the comment in the section on the clearing obligation, without entering into the details of the Brexit implications, there could be some changes on which derivatives traded in the UK qualify as OTC derivatives or not, which would then impact the calculation towards the clearing thresholds and thus possibly the scope of counterparties and contracts subject to the NFC+ requirements.

## 6 Conclusion

51. In the light of the temporary regime under MIFID II that allows NFCs+ trading C6 energy derivative contracts to benefit from an exemption from the clearing obligation and bilateral margining for these contracts and to exclude C6 energy derivative contracts from the calculation of positions for the purpose of the clearing thresholds, the report draws some conclusions on the impact of such regime.
52. The report assessed the potential benefits in terms of reducing counterparty risk and systemic risks of making C6 energy derivative contracts subject to certain EMIR requirements by focusing on the impact of applying the clearing obligation, the requirement to exchange collateral and including C6 derivative contracts in the calculation of positions for the purpose of the clearing obligation.

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<sup>26</sup> ESMA clarified further when to notify ESMA and how to calculate positions for the purpose of the clearing obligation in the OTC Q&A 2 in the Q&As for the implementation of EMIR: [https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52\\_qa\\_on\\_emir\\_implementation.pdf](https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf)

53. The first factor to consider is that NFCs represent a large part of the commodity derivative market and that in many cases they enter into commodity derivative transactions for hedging purposes, including C6 energy derivatives. The second factor to bear in mind is that this market is much smaller in relative terms compared to the rest of the derivatives market. Both factors thus lead to the conclusion that there does not seem to be an urgency to change the regulatory regime for C6 energy derivatives with regards to EMIR from a systemic risk perspective.
54. In addition, the report also shows that changing the regime for C6 energy derivatives with regards to the clearing obligation, the requirement to exchange collateral and the calculation towards the clearing thresholds is not expected to have an immediate major impact, thus questioning the actual benefits of changing the regime now.
55. Finally, the report also highlighted that in view of the context with the withdrawal of the UK from the European Union, as an important share of the C6 energy derivatives contracts are either traded or cleared in the UK and that there is some uncertainty on how the regulatory framework might evolve there, it would be more prudent to wait before considering a change in the regime.
56. Taking all of the above into account, ESMA does not see the need to change the regulatory framework now with regards to C6 energy derivative contracts and some of the EMIR requirements. Consequently, ESMA would recommend extending the temporary regime for C6 energy derivative contracts as is foreseen in MiFID.