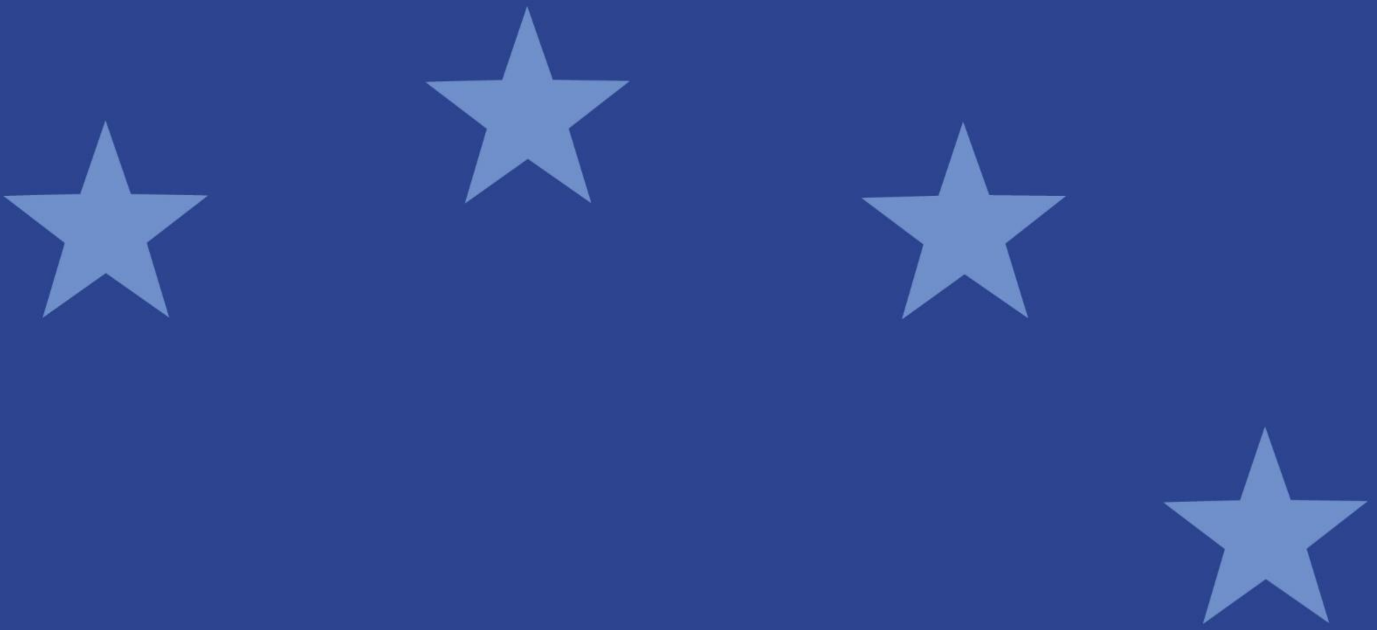
Final Report

EMIR RTS on the commodity derivative clearing threshold



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Executive Summary

Reasons for publication

The “EMIR Refit” Regulation ((EU) 2019/834) introduced a mandate in EMIR for ESMA to periodically review the clearing thresholds (CT) and propose to update them where necessary, in order to ensure that the CTs remain appropriate. Following this review and where an amendment of the CTs is identified as necessary, then ESMA can submit regulatory technical standards (RTS) proposing new values for the CTs. This report is presenting the amending RTS proposing to change the CT for commodity derivatives.

ESMA conducted a review of the CTs which was described in a discussion paper (DP) published on 21 November 2021 and ran a public consultation until 19 January 2022. The DP included a section on one important and time sensitive issue facing non-financial counterparties (NFCs) entering into commodity derivatives, in particular energy firms. Following Brexit, EU NFCs have explained about being constrained by the CTs since their derivatives executed on UK markets now count towards the CTs. This issue has become more important with the rise in energy prices this past winter and has since become even more acute due to the war in Ukraine.

Fundamentally, ESMA believes that the CT framework needs to be amended to better recognise the benefits of clearing. ESMA has thus recommended in its high-level response to the European Commission (EC) consultation on the targeted review of EMIR, that instead of distinguishing between OTC and Exchanged Traded Derivatives (ETD, including derivatives executed on third-country markets not deemed equivalent) for the purpose of the CTs, the distinction should be between cleared versus non-cleared, such that only derivatives not cleared at an authorised or recognised CCP should count towards the CTs.

In the meantime, and in order to alleviate temporarily the impact of the current energy prices on NFCs, ESMA has developed an RTS proposing to increase the CT for commodity derivatives by EUR 1 billion. Once the EMIR framework review is finalised, ESMA will re-assess the CTs based on the new methodology, including the applicable CT for commodity derivatives. However, ESMA stands ready to review the level of the CT at any point in time should the conditions change. Lastly, this report focuses on this particular aspect of the CT review for which there is urgency to act, whereas the rest of the feedback to the DP will continue to be handled as part of the broader workstream looking at the regular review of the CTs.

In preparing this report, ESMA took into account the feedback from the public consultation on the DP, consulted the European Systemic Risk Board (ESRB) and requested the advice from the Securities and Markets Stakeholder Group (SMSG).

Content

This report presents the implications of exceeding the CTs, the details of the feedback received on the DP and the proposed amendment.

Next Steps

The draft RTS presented in the Annex are being submitted to the EC for endorsement in the form of a Commission Delegated Regulation, i.e. a legally binding instrument directly applicable in all Member States of the European Union. Following their endorsement, they are subject to non-objection by the European Parliament and the Council.

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1 Introduction

1. EMIR and the various RTS on the clearing obligation (CO)[1] set up the regulatory framework for the CO in the European Union (EU) and the European Economic Area (EEA). Regulation (EU) 2019/834 (referred to as EMIR Refit)[2], modified certain aspects of the clearing regime and introduced a mandate for ESMA to periodically review[3] the CTs and, when necessary, propose amendments to update them. The aim of such reviews is to ensure that the thresholds remain appropriate and take account of any material changes in financial markets.

2. To fulfil this mandate ESMA published a DP on the Review of the CTs in November 2021 and publicly consulted until 19 January 2022. The paper assessed the coverage of the current CTs per asset class, both in terms of notional cleared and in terms of market participants dealing with OTC derivatives that were subject to the CO, to review whether the CTs remain well-calibrated.

3. In addition, the paper included considerations with wider implications on the EMIR framework that are intertwined with the discussion on the CTs calibration and merit attention. Some of those aspects focused on the equivalence system with regards to third-country markets that are or are not determined as equivalent under EMIR and the calculation methodology for determining which counterparties are above or below the CTs. Further, the paper looked into other broader aspects, such as the overall effectiveness of EMIR and how it is positioned from a comparative perspective in relation to other jurisdictions with similar regulatory frameworks.

4. In parallel, some energy firms' associations also reached out to ESMA to voice their concerns regarding different aspects of the EMIR framework impacting their trading activity in commodity derivatives. Those concerns relate to the consequences of Brexit, the calculation methodology to determine which NFCs are above the CTs (therefore subject to the CO and to bilateral margin requirements), the scope of the hedging exemption and the increase of commodity prices. The DP included a section on this aspect in order to receive input on these issues from a wide range of stakeholders, including from energy firms.

5. The feedback received to the DP brought some valuable input for the review of the CTs, but also of the overall EMIR framework in the context of the Consultation on the targeted review of the central clearing framework in the EU conducted by the EC.

6. It should be noted that ESMA submitted on 5 April 2022 a high-level response to the Consultation providing input on a variety of issues. Notably, ESMA's response included

[1] Commission Delegated Regulation (EU) 2015/2205 of 6 August 2015 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on the clearing obligation (OJ L 314, 1.12.2015, p. 13); Commission Delegated Regulation (EU) 2016/592 of 1 March 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on the clearing obligation (OJ L 103, 19.4.2016, p. 5); Commission Delegated Regulation (EU) 2016/1178 of 10 June 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on the clearing obligation (OJ L 195, 20.7.2016, p. 3).

[2] Regulation (EU) 2019/834 of the European Parliament and of 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 (OJ L 141, 28.5.2019, p. 42). EMIR consolidated text can be found here: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02012R0648-20210628.

[3] Article 10(4) of EMIR.

two structural change proposals to the EMIR CT framework that are interlinked and relevant for this report:

7. The first one, with regards to the current CTs methodology framework, proposes to shift from the current definition of ETD vs OTC (where ETDs are not included in the calculation and OTC derivatives are), to adopt a cleared vs uncleared distinction, to only count non-centrally cleared derivative contracts for the purpose of calculating positions for the CTs.

8. The second one refers to bilateral margins and proposes to apply them to NFCs above the clearing threshold (NFC+) on a "per-asset-class-basis", i.e. once the relevant threshold is exceeded. This change will be aligning the approach for bilateral margin requirements for NFCs with the approach for the CO (where NFCs become subject to the CO only for the classes of derivatives in the asset class for which they exceed the CT[4]).

9. This Final Report takes into account these Level 1 change recommendations and presents an overview of the considerations, concerns and feedback on the aspects related to the issues faced by NFCs entering into commodity derivatives. If the proposed amendments to Level 1 are adopted, ESMA will re-asses the CTs as part of the mandate to periodically review them, to ensure they remain fit for purpose.

10. Finally, this report includes the proposal amending the RTS on the CTs[5] in order to increase the CT for commodity derivatives by €1bn.

2 The implications of exceeding the CTs

2.1 Clearing obligation

11. As explained in the DP, EMIR Refit maintained the asset classes subject to mandatory clearing and the procedure to determine which classes are fit for the CO unchanged. Currently, the CO applies to certain types of credit derivatives and interest rate derivatives (IRDs)[6].

12. However, EMIR Refit changed the methodology to determine which counterparties are subject to the CO and for which asset classes. More specifically, EMIR Refit modified the use of the CTs, triggering the CO only when a financial counterparty (FC) or an NFC exceeds them, based on specific calculation methodologies.

13. In particular, to determine whether a counterparty exceeds the CTs, EMIR establishes that both FCs and NFCs will calculate their aggregate month-end average position in OTC derivative contracts for the previous 12 months. FCs and NFCs have different

[4] Assuming there is a clearing mandate for those. Currently the CO applies to certain types of interest rate derivatives and credit derivatives.

[5] As specified by Commission Delegated Regulation (EU) No 149/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on indirect clearing arrangements, the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP (OJ L 52, 23.2.2013, p. 11).

[6] ESMA maintains a centralised Public Register which centralises information on the asset classes and types of derivatives contracts subject to the CO:
https://www.esma.europa.eu/sites/default/files/library/public_register_for_the_clearing_obligation_under_emir.pdf

ways to calculate their positions, as established by Article 4a and Article 10 of EMIR, respectively. Notably, on the one hand, FCs include in their calculation all OTC derivative contracts entered into by any entity within their group (this refers to all FCs and NFCs within the same group) and, on the other hand, NFCs only include OTC derivative contracts entered into by the NFCs within the group.

14. In addition, NFCs benefit from the so-called hedging exemption whereby OTC derivatives that are entered into to reduce risks related to their commercial activity are excluded from the calculation of positions towards the CTs. The EMIR framework provides criteria to establish which OTC derivative contracts are to be considered as hedging transactions, which include the accounting definition of hedging based on International Financial Reporting Standards (IFRS) rules, as well as proxy hedging and portfolio hedging.

15. Regarding the calculation of positions towards the CTs, EMIR offers the possibility for counterparties to choose not to calculate their positions. In that case, they will be considered subject to the CO. Entities have to notify ESMA and their national competent authority (NCA) when the result of their calculations exceeds the CTs or where they choose not to calculate.

16. Another element to consider is that NFCs, when exceeding a CT become subject to clearing only for the asset class/es in which their positions are above the CT rather than for all asset classes. For instance, if an NFC exceeds the EUR 3 billion threshold for credit derivatives, it becomes subject to the CO for its credit derivative trades but does not become subject to the CO for its IRDs (unless it also exceeds the CT for IRDs). In contrast, when an FC exceeds a single CT, it becomes subject to the CO for all its asset classes (for which there is a mandate to clear).

2.2 Bilateral margins

17. FCs and NFCs entering into non-cleared OTC derivative contracts have to comply with the risk-mitigation techniques described in Article 11 of EMIR, ensuring that they have procedures and arrangements to mitigate counterparty credit risk, including at least timely confirmation, portfolio reconciliation, dispute resolution and valuation of outstanding contracts. In addition, FCs and NFCs+ shall mark-to-market on a daily basis the value of outstanding contracts and should comply with the requirement to exchange collateral (bilateral margins).

18. Under EMIR, FCs and NFCs+ are subject to the bilateral margin requirements, whereas NFCs- are not. When FCs and NFCs+ are above the EUR 8 billion threshold set in the RTS on bilateral margins[7], then the bilateral margin requirements also include the initial margin requirements. The RTS on bilateral margins contains a phased implementation of the initial margin requirements (according to a calendar agreed at the international level), with the last phase scheduled for September 2022, which will then capture all counterparties above the EUR 8 billion threshold.

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[7] 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).

19. This means that for FCs, exceeding the CTs only has an impact with respect to the clearing obligation as they are subject to the risk mitigation techniques, including bilateral margining (initial margin only when meeting the additional conditions explained in paragraph 18), in all cases, i.e. whether they are above or below the CTs.

20. Whereas for NFCs, exceeding the CTs has an impact with respect to the clearing obligation and also with respect to bilateral margins. When an NFC exceeds any of the CTs and becomes NFC+, this triggers the clearing obligation in that asset class, and it also triggers the bilateral margin requirements for all its uncleared OTC derivatives (initial margin requirements only when meeting the additional conditions explained in paragraph 18).

21. More specifically, this means that NFCs+ must post variation margin for non-cleared derivatives from the moment they become NFC+, and initial margin according to the phase-in established in the RTS on bilateral margins (depending on their aggregate average notional amount of non-centrally cleared derivatives).

22. Contrary to the approach "per asset class" followed under the CO, where an NFC+ becomes subject to the CO only for the asset classes it has exceeded the CT for (currently there is only a CO for certain IRDs and credit derivatives), an NFC+ becomes subject to the bilateral margin requirements for all its non-cleared OTC derivatives. This aspect has raised some concerns among respondents to the DP as they consider it to be disproportionate. Annex III provides an example of the costs of complying with these risk mitigation requirements for NFCs becoming NFCs+, as provided by the European Federation of Energy Traders (EFET) and some of its members in the feedback to the DP.

23. Another aspect raised in the feedback related to the difference in the approaches taken in EMIR for the CO and for bilateral margins is the lack of a specific preparatory time (or grace period) to start complying with the bilateral margin requirements. EMIR foresees a 4-month period to start clearing after counterparties exceed the CT, while such preparatory period does not apply to the bilateral margin requirements. In this sense, some respondents argue that setting up the procedures needed to comply with all risk mitigation techniques, including the bilateral margin requirements can take up to 12 months of preparation.

2.3 Impact

24. The following table illustrates the changes introduced in EMIR by EMIR Refit regarding the impact of the CTs on the CO and the risk mitigation techniques for FCs and NFCs:

Figure 1:

	EMIR		EMIR Refit	
	FCs	**NFCs**	**FCs**	**NFCs**
CTs	Not applicable	EUR 1 billion: credit and equity derivatives EUR 3 billion: IRDs, FX and commodity derivatives	***New:** Same CTs as NFCs but some differences (e.g. no hedging exemption)	Same as before
Entities subject to the CO	All FCs	NFCs+ (excluding hedging)	***New:** Only FCs above CT	Same as before
Asset classes to clear	All asset classes for which there is a CO	For NFCs+, all asset classes for which there is a CO.	For FCs+, all asset classes for which there is a CO	***New:** For NFCs+, only asset classes for which the CT is exceeded and for which there is a CO.
Risk mitigation techniques excluding bilateral margins	All FCs	All NFCs	Same as before	Same as before
Bilateral margins	All FCs (initial margin when above the EUR 8 bn threshold)	NFCs+ (initial margin when above the EUR 8 bn threshold)	Same as before	Same as before

25. Following from the above, FCs becoming FCs+ need to prepare to clear their OTC derivatives in scope of the CO. For NFCs becoming NFCs+, they may have to put in place clearing arrangements for the asset class for which they exceed the CT and they need to start complying with the bilateral margin requirements for all their uncleared OTC derivatives, which can represent a significant undertaking for some of them, in terms of compliance costs and amount of collateral to post.

3 Issues raised by firms in the energy sector trading commodity derivatives

26. Trade associations from the energy sector, first EFET and then more broadly the Joint Energy Associations Group (JEAG), have raised to ESMA's attention the issues some energy firms are facing with respect to the current CT framework.

27. They flagged the impact on the CTs calculations and the potential implications for EU energy firms, of the absence of an equivalence decision under Article 2a of EMIR for UK markets (in particular ICE and LME). More broadly, they also raised some concerns on the wider EMIR CT framework, arguing that the EU CT framework was stricter than that of a number of other key jurisdictions' regulatory regimes and thus that it was affecting EU entities' (mainly NFCs) ability to compete, to hedge and to contribute to the green energy transition.

28. They conducted a comparative assessment of the regulatory regimes applicable to NFCs with respect to OTC derivatives in various jurisdictions, including EMIR and other third-country legal and regulatory frameworks (mainly the US, Australia and Singapore)[8]. The objective of the comparative assessment was to show that EMIR appears as the strictest framework, not only due to the levels at which the CTs are set, but also because of the entities and instruments within the scope of the calculation.This assessment was accompanied by an estimation of the costs that an NFC would incur to comply with complementary requirements if it exceeded any of the CTs (see Annex III).

29. However, more details should be taken into account to conduct an exhaustive and conclusive comparison as there are some significant differences of the frameworks in the respective jurisdictions. For example, in the case of Australia, neither non-financial market participants nor physical instruments seem to be in scope, while in the case of Singapore, the clearing mandate seems to apply only to licensed banks above a CT of SGD 20 billion.

30. Following from this, these energy firms associations advocate for changing the CT framework and to increase the CT for commodity derivatives.

31. The DP included a section on this area of concerns such that ESMA could also hear the views from a broader range of stakeholders on this particular issue. As a result, ESMA has looked into the arguments raised by the energy firm associations together with the further feedback received to the DP, i.e. from other associations and individual entities from different sectors of activity. The following section covers the feedback received on these specific aspects.

[8] EFET commissioned this assessment to a law firm and provided ESMA the document and it was also part of EFET's feedback to the DP.

4 Feedback received to the discussion paper on the review of the CTs[9]

32. ESMA's public consultation on the DP ran from 22 November 2021 to 19 January 2022. A total of 29 respondents provided feedback[10], out of which 9 FCs, 19 NFCs and one academic. Sixteen out of the 19 NFC responses came from the energy industry and all of them (except for one) have presented roughly the same arguments that the energy firm trade associations had previously sent to ESMA. The responses to the consultation can be found on ESMA's website[11]. The following section focuses on the feedback related to the issues faced by energy firms entering into commodity derivatives.

4.1 Lack of equivalence of third-country markets and Article 2a of EMIR

33. Almost all NFCs responding to ESMA's DP raised concerns with regards to Brexit and more generally, to the lack of equivalence under Article 2a of EMIR, notably for ICE and LME.

34. Energy firms argue that ICE and LME are the most liquid pools for some instruments, e.g. coal, metals, oil and other commodity products listed on these venues. Currently, these respondents do not find alternative trading venues with a comparable product offering and liquidity in the EU or elsewhere, making ICE and LME the commercially most attractive venues. They mention that access to these markets is thus essential for efficient hedging of long-term supply contracts (such as gas and LNG). Hence, EU NFCs explain depending on their access to ICE and LME to efficiently trade and hedge these commodity derivatives[12].

35. The EC has not adopted an implementing decision declaring UK trading venues equivalent to an EU regulated market under Article 2a of EMIR. Without an equivalence decision, the derivative contracts executed on UK Markets (which were EU regulated markets before Brexit) and continue to be cleared by recognised CCPs, as from January 2021 qualify as OTC.

36. Consequently, these OTC contracts must be included in the calculation of counterparties' positions against the CTs (unless the hedging exemption applies), and this has an impact on entities that may suddenly become subject to the CO and bilateral margins.

37. As mentioned in the introduction, ESMA has recommended in its high-level response to the EC consultation on the targeted review of EMIR to change the CT framework, in particular to only count derivatives not cleared at an authorised or recognised CCP. With this approach, the CT calculation would depart from the current approach based

[9] https://www.esma.europa.eu/sites/default/files/library/esma_70-156-5010_review_of_the_clearing_thresholds_under_emir.pdf
[10] We have included associations representing FCs and NFCs views respectively in the count.
[11] Discussion paper on the review of the clearing thresholds under EMIR (europa.eu)
[12] EFET feedback Annex forbearance letter 11032021, included as attachment to their response to ESMA.

on the OTC derivative definition and the need for an equivalence decision under Article EMIR 2a of EMIR.

4.2 Framework for the calculation of positions

38. Several respondents raised the issue that the methodology in EMIR for calculating positions towards the CTs including all entities in the group (also those in non-EEA countries) puts them at a competitive disadvantage when compared to the framework in other jurisdictions, including the US regulatory framework. They argue that these other jurisdictions use different calculation methods, based on dealing activity rather than on outstanding positions. These respondents would favour a calculation which follows a methodology similar to the one in the U.S.

39. The energy industry respondents have insisted on the fact that in the case of the U.S., the Dodd-Frank Act includes in the calculation only swaps entered into within the preceding 12 months, therefore outstanding maturities from older transactions would not be included in the calculation. More detailed information provided by one of the respondents (Commodities Market Council Europe) indicates that the calculation of CTs for NFCs that maintain a substantial position in swaps is also more complex, as it factors in open exposure and notional amounts. According to the information provided by this respondent, due to the combination of open exposure and potential future exposure (which is based on the notional, type and residual maturity of the transaction) the CT for commodity swaps with less than one-year residual maturity in the U.S. would allegedly be “essentially equivalent to a notional threshold of up to USD 20bn”. In the EU, the calculation is based on gross notional value and indeed it includes the outstanding notional exposure of e.g. a 10-year OTC swap during its entire duration, contrary to what would be counted by U.S. entities.

40. In addition, several respondents have explained that, outside the EU, the ability of their subsidiaries to compete with local entities in countries such as the US and Australia is also limited by the level of the CT for commodity derivatives set in EMIR. In some cases, as described by some respondents from the energy sector in their responses, some jurisdictions do not include NFCs when regulating trading on derivatives and the CO.

41. ESMA considers that there is merit in having a holistic approach in the calculation methodology and to include outstanding positions (reflecting to some extent the level of outstanding risk) rather than the “dealing” activity. At the same time, ESMA takes note of the feedback received and agrees that amending some aspects of the EMIR calculation framework could have a positive impact in terms of competitiveness of EEA entities outside the EEA and boost EMIR effectiveness, while still preserving risk mitigation safeguards. As mentioned in the introduction, ESMA expressed support for amending the CT framework in its high-level response to the EC consultation on the targeted review of EMIR.

4.3 Hedging and the scope of the exemption

42. The energy industry respondents explained in their feedback to the DP that the transition towards a more decarbonised energy system, and the development of renewable energy sources that goes with it, trigger very high demands for hedging. Renewable energy producers enter into OTC financial contracts (including fix-to-float

swaps) with traditional energy producers to ensure a fixed revenue despite the intermittent nature of their energy output (especially in the case of wind and solar power). These OTC contracts are negotiated bilaterally to respond to the specific needs of each producer and have very long maturities (10 to 20 years). Therefore, there appear to be no real alternatives in more standardised exchange-traded contracts.

43. The energy industry expressed that in the course of their business they enter into OTC financial contracts with some of their clients in order to allow their clients to hedge risks emerging from the clients' commercial activity. The hedging exemption does not cover all trading activities as hedging is limited to specific risk reducing activities covering eligible underlying commercial activities only. Consequently, according to energy firms, all risk reducing transactions with financial or speculative underlyings do not fall under the hedging exemption.

44. In the particular case of the production of renewable energy, respondents have mentioned Power Purchase Agreements (PPAs) as widely used means of investment financing and hedging for renewable energy producers. These PPAs ensure that the renewable energy producer obtains a fixed margin for the produced power. In this case, the entity providing the hedge takes a risk which then it hedges with other derivative contracts. Secondly, the energy industry has explained that in order to cover their commercial activities they sometimes enter into hedging transactions in a currency other than the one in which the group finances itself and they subsequently use FX transactions to reduce currency risks arising from the hedging transactions in different currencies.

45. According to respondents to the public consultation, in both situations, i.e. when hedging risks emerging from a financial transaction which is not a hedge and when further hedging currency risks emerging from a financial transaction which is a hedge, they cannot consider the new transaction as a hedge and have to count them in the calculation of positions for the CTs. According to the respondents, the current CT for commodity derivatives would not be enough to accommodate these needs.

46. Some of the respondents from the energy industry have pointed more concretely to the German auditing standard on EMIR which states that "the underlying transactions in the portfolios must originate from the operational business of the company and may not be derivative contracts within the meaning of MiFID II", that they consider as being too restrictive. Similarly to the feedback received from commodity trading firms, ISDA and FIA also mention the German supervisory regime for NFCs as being stricter due to their auditing standard and they argue that this could give rise to an unlevel playing field across member states.

47. In contrast, Deutsche Börse Group (DBG) highlights in its feedback to ESMA the importance of narrowing down the hedging exemption to only cover true commercial hedging and treasury financing activities.

48. The respondents asking for a clarification of "commercial activity" suggested an ESMA Q&A to ensure that the scope of hedging covers the financial transactions described above.

49. ESMA is of the view that interpreting "commercial activity" in the context of the EMIR hedging exemption along the lines suggested by some respondents might have broader implications, as it could mean that for an energy trading entity, providing a

financial service is a simple "commercial activity". However, this type of activity is framed by MiFID II and the ancillary activity exemption[13].

50. In addition, the second case provided as an example by respondents (i.e. covering their commercial activities by entering into hedge transactions in a given currency and then using FX swaps to reduce currency risks) could be considered as covered by the current hedging exemption in some EEA jurisdictions. For these reasons, to ensure the current application of the hedging exemption does not create an unlevel playing field, ESMA sees merit in further investigating this issue and providing relevant guidance.

4.4 Rise of commodity prices and the need for a recalibration of the CTs

51. In the feedback to the DP, respondents from the energy sector (with the support in this case of the two associations representing corporate treasurers[14]) highlighted the impact of inflation on their ability to continue operating without breaching the CTs. The year 2021 was indeed marked by a high increase of commodities' prices.

52. This inflation means in the case of energy firms, and also for other corporates, that with the same amount of gross notional value in derivatives they can actually do less business. Some of the arguments point at the fact that the EMIR CTs were established in 2012 and that compared to the prices in 2021, gas, power and EUAs have increased considerably. Hence, the level of the CT for commodity derivatives does not give enough room to NFCs to navigate present and future price volatility. Furthermore, NFCs could potentially passively exceed the CT because of the continued rise of commodity prices.

53. For these reasons, some respondents asked for a review of the CT for commodity derivatives as in their view, these aspects have factually lowered the CT for commodities, which numerically remained unchanged. In particular, they asked for a EUR 1 billion increase of the CT for commodity derivatives to compensate for such increases in prices.

54. In contrast, DBG considers that the current CTs have proven useful and appear to be well-calibrated. Therefore, DBG would not see the need for any substantial changes to the level of the CTs in relation to commodity derivatives. In addition, DBG notes that the main criterion to be considered for reviewing a CT should be the systemic risk a market participant brings to the market. In their view, due to the high market volatility in the commodities business since the start of the Covid-19 pandemic, with considerable

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[13] Article 2 of 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. 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 determine whether those activities cannot be considered ancillary and therefore the counterparty needs to obtain authorisation as an investment firm.

[14] The two associations representing corporate treasures who have replied to the DP did not ask for an increase of the CTs due to inflation.

price movements within days or hours there is an increased need for energy traders to clear their transactions via a CCP to mitigate counterparty risk.

55. Further, the two associations representing corporate treasurers consider that the current CTs across asset classes are well-calibrated for NFCs and see a risk in introducing new requirements for NFCs in terms of liquidity management.

56. Similarly, the Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) and the Swedish Securities Markets Association (SSMA) indicate in their responses that based on the data available, the current CTs are appropriate across asset classes, and the latter strongly recommends not changing them.

57. First of all, in this report, as explained in the introduction, ESMA focuses on the CT for commodity derivatives, given the urgency to act on this. Some of this feedback related to the other CTs and this will continue to be handled in the broader workstream looking at the regular review of the CTs.

58. Secondly, ESMA acknowledges the importance of the level of increase in prices in 2021 and also the recent impact of the Russian invasion of Ukraine on commodity market prices. As developed further in its high-level response to the EC consultation on the targeted review of EMIR, first and foremost, ESMA advocates for a change of the CT framework. In the meantime, taking into account the time that it will take for the changes proposed to the EMIR framework to be adopted, and in order to alleviate the issues faced by NFCs linked to the important increase in commodity prices, ESMA sees merit in recalibrating the CT for commodity derivatives and to increase it by EUR 1 billion to allow market participants dealing with commodity derivatives to continue performing their activity not being disproportionately impacted by the current increase in commodities' prices.

5 RTS amendment to increase the CT for commodity derivatives

59. As developed in the high-level response to the EC consultation on the targeted review of EMIR, ESMA proposed measures to amend the CT framework, which would address several aspects discussed in this report.

60. However, the EMIR Review will take some time to be finalised. According to the feedback received, in the current situation a number of entities are limiting their activity to avoid exceeding the CT due to the impact of Brexit and the rise of commodity prices. Bearing in mind the costs this brings (especially with regards to bilateral margining for NFCs), the situation calls for some immediate actions.

61. In view of this, ESMA proposes to increase the CT for commodity derivatives by EUR 1 billion (from the current EUR 3 billion to EUR 4 billion). This should alleviate some of the concerns expressed by market participants while the EMIR amendments are being discussed, finalised and then adopted. Once EMIR has been amended, then ESMA would conduct a new calibration of the CTs based on the new methodology.

62. ESMA included in the DP a number of general questions on the coverage of the CTs and also a specific one for commodity derivatives and its different impact on FCs and NFCs. Given the urgency of the change to increase the CT for commodity derivatives by EUR 1 billion, no additional public consultation is launched on the revised draft RTS. However, this is a targeted change and these feedback collected by ESMA in the context of the DP's public consultation informed it, as it was a proposal from many respondents.

63. In addition, in accordance with EMIR, ESMA consulted the ESRB on the amending RTS to increase the CT and also requested the advice from the SMSG.

64. The ESRB, in their response (cf. Annex V), expressed concerns regarding the increase of the CT for commodity derivatives. However, the ESRB agreed that the current extraordinary market circumstances can call for measures to avoid unintended negative implications and recommended an increase in the CT for commodity derivatives to be for a short, predefined time and that it should be accompanied by a deadline.

65. ESMA acknowledges the ESRB concerns and sees increasing the CT for commodity derivatives as an interim solution that can help EU counterparties remain competitive while the changes that ESMA proposed to the Level 1 framework are incorporated. Given the uncertainties around the timing of the legislative procedure on the Level 1 framework, ESMA does not recommend a pre-defined end date for this increased CT. However, in view of the ESRB opinion, ESMA stands ready to review the level of the CT at any point in time should the current market conditions change.

66. Furthermore, the ESRB indicates that energy traders have recently been voluntarily switching from OTC markets to centrally cleared markets as the counterparty risk is currently very high among their peer group, which would reduce the need for this threshold increase. ESMA has no evidence of this, while on the contrary, following Brexit, the change in the legal qualification of ETDs concluded on UK markets has increased the share of derivative contracts considered OTC included in the calculation of positions towards the CTs.

67. With regards to the SMSG, no objection was raised and a few subject matter experts from the SMSG expressed full support for the clearing threshold increase for commodity derivatives.

6 Conclusion

68. ESMA has detailed measures to amend the CT framework to better recognise the benefits of clearing in its high-level response to the EC consultation on the targeted review of EMIR. In the meantime, after having analysed the feedback received and in view of the circumstances described in the report, in particular the sharp increase in commodity prices, ESMA is proposing to increase the CT for commodity derivatives.

69. The increase of the CT for commodity derivatives to EUR 4 billion should be adopted without delay while other more structural changes that require amendments to EMIR are being considered. ESMA will continue monitoring the coverage of the CTs, in line with the EMIR mandate to periodically review the CTs and changes in market conditions, to ensure that they remain well-calibrated.

Annex I: Commission mandate to develop technical standards

Article 10(4) of Regulation (EU) No 648/2012

Non-financial counterparties

In order to ensure consistent application of this Article, ESMA shall develop draft regulatory technical standards, after consulting the ESRB and other relevant authorities, specifying:

(a) criteria for establishing which OTC derivative contracts are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity referred to in paragraph 3; and

(b) values of the clearing thresholds, which are determined taking into account the systemic relevance of the sum of net positions and exposures per counterparty and per class of OTC derivatives.

After conducting an open public consultation, ESMA shall submit those draft regulatory technical standards to the Commission by 30 September 2012.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1095/2010.

After consulting the ESRB and other relevant authorities, ESMA shall periodically review the clearing thresholds referred to in point (b) of the first subparagraph and, where necessary taking into account, in particular, the interconnectedness of financial counterparties, propose to amend the regulatory technical standards in accordance with this paragraph.

That periodic review shall be accompanied by a report by ESMA on the subject.

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Annex II: Draft Technical Standards

COMMISSION DELEGATED REGULATION (EU) …/..

of [ ]

amending the regulatory technical standards laid down in Delegated Regulation (EU) No 149/2013 as regards the value of the clearing thresholds for commodity derivatives

(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[15], and in particular Article 10(4), third subparagraph, thereof,

Whereas:

(1) Commission Delegated Regulation (EU) 149/2013[16] specifies, among others, the values of the clearing thresholds for the purpose of the clearing obligation.

(2) Pursuant to Regulation (EU) No 648/2012, the European Securities and Markets Authority (ESMA) shall periodically review the clearing thresholds after consulting the European Systemic Risk Board (ESRB) and other relevant authorities and, where necessary taking into account, in particular, the interconnectedness of financial counterparties, propose to amend the relevant regulatory technical standards.

(3) The United Kingdom became a third country on 1 February 2020 and Union law ceased to apply to and in the United Kingdom on 31 December 2020. Outstanding derivative contracts executed on regulated markets in the United Kingdom before Union law ceased to apply to and in the United Kingdom remained exchange traded derivatives and therefore did not count towards the clearing thresholds. Thus, absent any relevant equivalence decisions pursuant to Article 2a or Regulation (EU) No 648/2012, only new contracts executed on markets in the United Kingdom after Union law ceased to apply to and in the United Kingdom are considered OTC and, while being cleared by recognised CCPs, do count towards the clearing thresholds. However, those outstanding derivative contracts remaining exchange traded derivatives are reaching maturity and being replaced by new derivatives which are OTC and thus now count towards the clearing thresholds.

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

[16] Commission Delegated Regulation (EU) 149/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on indirect clearing arrangements, the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP (OJ L 52, 23.2.2013, p. 11).

(4) The recent increase in commodity prices, which increase was significantly exacerbated by Russia's large-scale invasion of Ukraine, have further impacted the competitiveness of Union counterparties dealing with commodity derivatives and requires amending the clearing threshold value for the purpose of the clearing obligation for commodity derivatives from EUR 3 billion to EUR 4 billion.

(5) Delegated Regulation (EU) No 149/2013 should therefore be amended accordingly.

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

(7) The amendment to Delegated Regulation (EU) No 149/2013 has an urgent character to allow counterparties to continue to develop their business strategy and remain competitive despite the move in prices. ESMA conducted an open public consultation on the substance matter of the level of coverage of the clearing thresholds for the different asset classes and specifically on the coverage for commodity derivatives asset class. Given the limited scope of the amendment and the urgency of the matter, it would be disproportionate for ESMA to conduct an additional open public consultation on the draft regulatory technical standards. ESMA consulted the ESRB in accordance with Article 10(4), fourth subparagraph, of Regulation (EU) No 648/2012 and requested the advice of the Securities and Markets Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council [(17)].

(8) In view of the recent increase of prices and its effect on counterparties entering into commodity derivatives contracts, it is necessary to provide market participants legal certainty as quickly as possible. This Regulation should therefore enter into force as a matter of urgency,

HAS ADOPTED THIS REGULATION:

Article 1

Amendment to Delegated Regulation (EU) No 149/2013

In Article 11 of Delegated Regulation (EU) No 149/2013, point (e) is replaced by the following:

"(e) EUR 4 billion in gross notional value for OTC commodity derivative contracts and other OTC derivative contracts not provided for under points (a) to (d)."

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*.

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[17] 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).

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]

Annex III: Cost estimation provided by JEAG for compliance with requirements due to changing status from NFC- to NFC+

	Example: European Commodity Trading Firm (Affected Departments: Legal, Back Office, Accounting, Finance & Treasury, Regulatory Reporting)	

Implementation
Collateralisation:
i) Variation Margin (VM)
ii) Initial Margin (IM)
iii) Locked Liquidity through posting of additional IM & VM
	6+ months
	
	9-12 months, covering both VM and IM
	
	10-12 months
	
	€ 1bn – € 2bn
		Back Office and Accounting:
		- Operational setup of same-day collateral management
		Finance & Treasury:
		- Treasury Management System: process and system enhancements for operational setup of same-day collateral management and payment process
		  - Setup of Custodian accounts and integration into Treasury Management System
		  - Alterations to core bank contracts
		Legal[1]**:**
		- Repapering of contracts
		- Renegotiation of Credit Support Annexes
		- Onboarding IM Custodian account
		
		Locked Liquidity: Additional collateral (IM & VM) to be posted with NFC+ and FC counterparties

Risk Mitigation Techniques:
i. Daily Reporting
  i. MTM per trade
  ii. Collateral
ii. Timely Confirmations
iii. Portfolio Reconciliation
iv. Portfolio Compression
v. Dispute Resolution
	6+ months
	
	3+ months for Reporting System changes
		Back Office and Accounting:
		- Credit Management System: updated workflow and changes to Trading System's End-of-Day processes
		- Daily portfolio reporting and dispute resolution
		- Portfolio compression and reconciliation support
		Regulatory Reporting:
		- Daily Mark-to-Market reporting and Automation of Interfaces to additional data sources
		- Reporting process and system upgrades to deal with increased data flow (> 20k trades/day)

Cost
i) Implementation
  i) Internal
  ii) External
ii) Ongoing (yearly)
	
	€ 1m - € 2m
	€ 4m - € 5m
	€ 11m - € 21m
		
		Internal: Legal & Project Management FTE, BO system costs, process and system enhancements, IT
		External: Legal consultants, process specialists, IT support, IT license costs
		Liquidity charge[3] + additional FTE in BO, Legal, Accounting, Finance and Regulatory Reporting

FTE[2] (cost included above)
i) Implementation
  i) Internal
  ii) External
ii) Ongoing
	
	14
	4
	10[4]
	5.5
		
		Legal repapering, Project Management, IT
		Legal consultants, process specialists, IT support
		Additional FTE: Back Office 2, Legal 0.5, Accounting 0.5, Finance 2, Reporting 0.5

[1] Assumptions: ca. 50 NFC+ or FC CPs, resulting in ~50 CSAs to renegotiate;
[2] FTE = Full-Time-Equivalent (Assumed costs: €200k/FTE);
[3] Assumption of €1m/year liquidity costs for every €100m in locked up liquidity;
[4] Reports from EU NFCs who moved to NFC+ suggest a project team of c.10 FTE for a full year

Annex 2: Collateralisation requirements of NFC+ according to Art. 11(3) EMIR, CDR 2016/2251 (RTS)

Summary overview only, for details see CVR 2016/2251. Further EMIR Requirements for NFC+ (Reporting, Risk Mitigation Techniques etc. to be reviewed separately)

EMIR Requirement	Content (Summary)	Where in RTS	Deptmts affected (preliminary assessment)	Remark	Time-to-implementation	Cost
General	NFC+ to establish, apply and document risk mgmt procedures (RMP) for exchange of collateral.	2(1)	Market Risk, Credit Risk Control, Credit Risk, Legal, Collateral Mgmt, Finance, Compliance, Treasury, Back Office, IT	RMP to cover all CPs, depending on respective status (FC+; FC-; NFC+ or NFC-) RMP may exempt NFC- from VM/IM, see Art 24 RTS; RMP may provide for further Threshold based exemptions, Art. 28/29 RTS or certain CPs (Covered Bonds, SPVs)	2-3 months	EUR 1mio
	Eligibility criteria of margin for non-cleard OTC derivatives	2(2)(a)	Risk, Coll Mgmt, Legal	Pre-defined (see Section 3 RTS): Cash, Bonds, Securities; NOT: PCGs		
	Calculation & Collection of margin	2(2)(b)	Coll Mgmt, Risk	Monitoring inherent risk of margin, no wrong-way risk, see Art. 4(2) RTS; Margin Credit Quality Assessment, see Art. 6, 7 RTS		
	Management and segregation of margin	2(2)(c)	Coll Mgmt	Pre-defined, see Section 5 RTS; IM: Segregation to be insolvency remote, but "quickly accessible" (external custodian needed)		
	Calculation of adjusted value of collateral	2(2)(d)	Coll Mgmt, Risk	Pre-defined, see Section 6 RTS		
	Exchange of information betw CP and authorisation and recording of exception of RMPs	2(2)(e)	Risk, Legal, Compliance			
	Reporting of exceptions to senior mgmt	2(2)(f)	Risk			
	Terms of Netting Agreements/Collateral Agmts	2(2)(g)	Legal	Pre-defined, see Art. 2(2) 2nd subpara (a)-(g), Art. 3 RTS; to be checked if EFETs/MNAs/CSA meet criteria, enforceability to be monitored		
	Periodic verification of liquidity of collateral exchanged	2(2)(h)	Risk	Challeging of bonds, securities etc. used		
	Timely re-appropriation of collateral in case of EoD of collecting CP	2(2)(i)	Risk, Legal	Entirely new legal set-up wrt IM (see below)		
	Regular monitoring of exposures of intragroup transactions	2(2)(j)	Risk	Intragroup margening may be excempt by application to NCA, but high requirements on centralised risk procedures, see Art. 32 etc. RTS		
	Independent Legal Review of enforceablity of Netting/Collateral Agmts	2(3)	Legal	Benchmark: Art. 296 CRR		
	RMPs to assess continous monitoring of enforceability of Netting/Collateral Agmts	2(4)	Risk, Legal	Continous monitoring of netting/collateral, per country of active business		
	Annual testing of risk mgmt procedures	2(5)	Risk			
	If IM Models used, documentation of RMPs and testing to be provided to NCAs upon request	2(6)	Risk			

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Variation Margin (VM)	VM Calculation daily, MTA to not exceed EUR 500k, Indept Amount = 0	9(1), 10	Treasury, Coll Mgmt	Time-zone adjustment (Art. 9(3) RTS)	6-9 months	EUR 1-2mio
	Definition of MtM Calculation Art. 10 RTS	10	Coll Mgmt, Risk			
	Same-day posting (exception: use of MPOR calculation, see IM)	12	Treasury, Coll Mgmt	Main challenge: current set-up: T+1/T+2 margin posting		
	VM for new (post CT-breach) transactions only	Art. 11(3) EMIR	Coll Mgmt, Risk (Credit Risk), Legal	To be determined: Split of portfolios in Legacy/New? Pro: No collateralisation of legacy portfolio Con: Operational burden, separation of netting sets may lead to increase of exposure		
			Coll Mgmt, Legal, Risk	Separation of EMIR derivatives for VM/IM margin needed?		
	Products exempt (if agreed w CP): Phy settled FFX, Phy settled FX Swaps	31a				
Initial Margin (IM)	IM to be held w third party custody, no rehypothecation or reuse	19	Risk, Coll Mgmt, Legal	Entire new operational set up, not (long) established in the market, high complexity wrt to operational interconnections and legal documentation	12+ months	EUR 3-4mio
	(Continuous) independent legal review to verify seggregation arrangements	19(6)	Legal			
	IM Calculation if	9(1), 11	Coll Mgmt			
	- new trade executed or expired, added to or removed from netting set - payment triggered under trade in netting set - if IM calculated w standard approach - if no calculation wihin 10 BDs		Risk, Coll Mgmt			
	IM Calculaton based on standard approaches and regulatorly approved models only	11(1), 16,17, 18 Annex IV	Risk, Coll Mgmt	Needs to be aligned w each CP, Art. 11(6) RTS		
	No offsetting	11(2)	Risk, Coll Mgmt, Legal			
	Same-day posting	13	Coll Mgmt	In case of dispute: split-the-difference		
	IM to be used	14	Risk, Coll Mgmt			
	Confidence interval and MPOR	15	Risk, Coll Mgmt			
	Products exempt: Spot FX, Phys settled FFX, Phys settled FX-Swaps, Principal of Currency Swaps	27				

Annex IV: Cost Benefit Analysis

Introduction

The values of the clearing thresholds were first established in Delegated Regulation (EU) No 149/2013, which entered into force in 2013. Recital 21 of that Regulation already indicated that they should be reviewed periodically. As explained in the introduction of this Report, EMIR REFIT further mandated ESMA to periodically review the CTs.

As a result of the first ESMA's consultation exercise on the review of the CTs with a DP, ESMA has identified arguments in favour of acting urgently in order to increase the value of the CT applicable to commodity derivative trading, on a temporary basis, in order to deal with the difficulties that real economy firms (in particular in the energy sector) currently face until ESMA's proposed measures with regards to the EMIR Level 1 framework can be taken into account and the review of EMIR enacted. If and when the changes to the EMIR framework would be enacted, a new assessment of the situation and a potential new recalibration of the CTs should be considered by ESMA.

Review of the clearing threshold for commodity derivatives

ESMA has considered two options: Option 1, not introducing any change to the value of the CTs; Option 2, increase the value of the CT for commodity derivatives on a temporary basis and by EUR 1bn.

Option 1 - EUR 3 billion in gross notional value for OTC commodity derivative contracts and other OTC derivative contracts not provided for under points (a) to (d) of Article 11 of RTS 149/2013.	
Costs	Reduced ability of commodity firms to trade in specific circumstances (e.g., providing hedging opportunities to renewable energy producers) without incurring significant costs due to bilateral margining requirements; Lack of hedging opportunities for entities relying on commodity firms to hedge the risks emerging from their commercial activity; If the CTs are exceeded (even in cases where the positions considered in the calculation result from cleared ETDs), then additional margin requirements applying to bilateral trading in all other asset classes which puts pressure on liquidity needs; Reduced competitiveness of EU commodity traders when competing with entities with similar business but based in other jurisdictions with higher clearing thresholds.
Benefits	It ensures that an important part of the notional on commodity derivatives held by NFCs (and by small financial counterparties) is subject to clearing or bilateral margining, hence there would be less risk to the market.

Option 2 - EUR 4 billion in gross notional value for OTC commodity derivative contracts and other OTC derivative contracts not provided for under points (a) to (d) of Article 11 of RTS 149/2013.	
Costs	- The proposed increase, although limited in value (only EUR1bn) and in time, will allow increased bilateral trading (including trading in non-recognised third-country venues) in commodity derivatives. Hence, an increase in the notional of commodity derivatives held by NFCs (and potentially small financial counterparties).
Benefits	- Increased hedging opportunities for entities benefiting from commodity firms to hedge their risks (e.g., renewable energy producers); - Increased competitiveness for EU commodity firms; - Alleviates financial constraints on commodity firms impacted by the lack of equivalence with regards to non-recognised third country venues where no alternative exists to trade similar commodity derivatives in the EU.

Preferred option

In view of the costs and benefits presented in this cost-benefit analysis and having regard to the different arguments presented in this Final Report, ESMA presented an RTS in line with Option 2. Furthermore, it is to be noted that this increase in the value of the CT for commodity derivatives should apply on a temporary basis, until the changes suggested by ESMA to the current EMIR level 1 framework are taken into account and the EMIR Review enacted. If and when those changes enter into force, ESMA will have to assess the CTs again in a holistic way.

Annex V: ESRB response

Ms Verena Ross
Chair of ESMA
European Securities Markets Authority
201-203 Rue de Bercy
75012 Paris
France

ECB-PUBLIC
ESRB/2022/0095

ESRB response to the proposed increase in the clearing threshold for commodity derivatives

6 May 2022

Dear Ms Ross, dear Verena,

I am writing to you with reference to ESMA's proposal to increase the clearing threshold for commodity derivatives by €1 billion, as the ESRB needs to be consulted on any changes to clearing thresholds.[1]

The ESRB appreciates ESMA's report on the European Market Infrastructure Regulation (EMIR) regulatory technical standard (RTS) concerning the commodity derivative clearing threshold.

In general, the ESRB agrees with ESMA that the clearing threshold framework needs to be amended in order to better respond to market or other developments and thus contribute more effectively to the growth of the clearing industry in the EU. For instance, the ESRB concurs with ESMA's view that, instead of distinguishing between over-the-counter (OTC) and exchange-traded derivatives (including derivatives executed on third-country markets not deemed equivalent) for the purpose of clearing thresholds, the distinction should be between cleared and non-cleared derivatives, such that only derivatives not cleared by an authorised or recognised central counterparty should count towards the thresholds. ESMA also suggested applying bilateral margins to non-financial corporations (NFCs) above the clearing threshold (NFC+) on a

[1] Article 10(4) of 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, Text with EEA relevance (OJ L 201, 27.7.2012, p.1).

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"per-asset-class basis", thereby aligning the approach for bilateral margin requirements for NFCs with the approach for the clearing obligation. This suggestion could be considered but warrants further analysis before any decision is taken. The ESRB believes that the forthcoming EMIR review will be a valuable opportunity to consider such changes in more detail.

The ESRB would, however, like to express some reservations regarding ESMA's proposal to increase the clearing threshold for commodity derivatives from €3 billion to €4 billion. While the ESRB understands ESMA's view that measures may be needed to mitigate the risks arising from the current extraordinary market circumstances, the ESRB is not convinced that increasing the clearing threshold would be the best course of action.

In particular, the ESRB wishes to emphasise that it believes that central clearing should be the preferred post-trade option. EMIR states in Article 10(4) that clearing thresholds "are determined taking into account the systemic relevance of the sum of net positions and exposures per counterparty and per class of OTC derivatives"[2]. There is no evidence that this systemic relevance has decreased. Indeed, it could be argued that the increase in market volatility of commodity prices since the start of the COVID-19 pandemic and, more recently, since the invasion of Ukraine, would point to a greater need for energy traders to clear their transactions via a central counterparty, to mitigate counterparty risk. More generally, the ESRB would like to reiterate that any adjustment to the clearing thresholds should be based on longer-term needs (such as inflation or other structural changes) rather than on short-term market developments. Adjustment of the clearing thresholds in response to market circumstances may create perverse incentives for market participants to request suspension of regulatory requirements whenever market situations give cause.

The ESRB would also like to ask ESMA to consider whether an increase in the clearing threshold is the most appropriate way to manage risks in the context of the broader clearing strategy for the EU and the capital markets union. In addition, energy traders have recently been voluntarily switching from the OTC markets to centrally cleared markets as the counterparty risk is currently very high among their peer group, which reduces the need for this threshold increase. The ESRB appreciates that ESMA plans to review the current methodology for calculating clearing thresholds and to solve the underlying issues in commodity and other markets, such as liquidity availability in the client clearing arrangements and the classification of futures.

[2] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32012R0648&from=EN

Against this background, the ESRB believes that any increase in the clearing threshold should be for a short, predefined time and should be accompanied by a deadline, which should allow the affected entities to prepare for meeting the clearing obligation and margin requirements once the temporary increase expires.

This letter was approved by the ESRB General Board in written procedure on 5 May 2022.

Yours sincerely,

Francesco Mazzaferro

Head of the ESRB Secretariat