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| 17 November 2021 |

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| Reply form for the Discussion Paper on the review of the clearing thresholds under EMIR |
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| Date: 17 November 2021 |

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the Discussion Paper on the review of the clearing thresholds published on the ESMA website.

*Instructions*

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

* use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
* do not remove the tags of type <ESMA\_QUESTION\_DP\_EMIR\_CTs> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
* if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

* if they respond to the question stated;
* indicate the specific question to which the comment relates;
* contain a clear rationale; and
* describe any alternatives ESMA should consider.

**Naming protocol**

In order to facilitate the handling of stakeholders’ responses please save your document using the following format:

ESMA\_DP\_EMIR\_CTs\_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

e.g. if the respondent were ESMA, the name of the reply form would be:

ESMA\_ DP\_EMIR\_CTs\_ESMA\_REPLYFORM

***Deadline***

Responses must reach us by **19 January 2021.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input - Consultations’.

***Publication of responses***

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

***Data protection***

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the headings ‘Legal notice’ and ‘Data protection’.

# General information about respondent

|  |  |
| --- | --- |
| Name of the company / organisation | EDF TRADING LIMITED |
| Activity | Non-financial counterparty |
| Are you representing an association? |  |
| Country/Region | UK |

# Introduction

Please make your introductory comments below, if any:

<ESMA\_COMMENT\_DP\_EMIR\_CTs>

The review of the EMIR clearing thresholds offers an opportunity to ensure the regulatory framework around derivative markets helps to facilitate the energy transition, enhance European competitiveness and improve market functioning, whilst safeguarding transparent and safe financial markets.

As part of the review, ESMA should evaluate the level of the EMIR clearing threshold for commodities (“EMIR CCT”) to ensure it is set at a systemic relevant level which will more closely align this regulatory tool with the underlying objectives of EMIR. The EU EMIR CCT is also significantly lower than other jurisdictions without any underlying justification. In addition, the global assessment of relevant activity against the EMIR CCT creates an extra jurisdictional reach for EU EMIR which is not contained in comparable legislation in any other jurisdictions. Together these factors severely limit participation in OTC derivative markets which reduces competition and increases the costs of hedging for a wide range of users who use derivatives as part of their risk management framework.

As such, we call for a significant increase in the EMIR CCT and a refocusing of the scope of the thresholds calculation so it only includes activity that is relevant to the functioning of the EU financial system.

This EMIR CCT increase and refocusing of its scope will help facilitate the energy transition and enhance European competitiveness by:

1. *Enabling more effective hedging -* By further enabling the development of open and competitive energy and commodity derivatives markets in the EU, it would enable energy firms to support the energy transition by providing liquidity to OTC markets and offering hedging opportunities to renewable energy producers and industrial consumers to reduce their commercial risks.
2. *Enhancing European competitiveness -* By aligning the EU regime with those in other jurisdictions subject to the same G20 commitments to regulate derivatives markets, it would enhance the competitiveness of European firms and enhance the development of euro-denominated energy and commodity markets. It is notable that the attached independent Benchmark Study on international best practice concluded that the EU EMIR regime applies the lowest clearing threshold applicable to the largest set of entities, products and activities.
3. *Ensuring high standards are maintained -* By safeguarding the EMIR goals of transparent and safe markets, our proposed review adheres to the aims of EMIR to make derivatives markets more transparent, to mitigate credit risk and to reduce operational risks.

<ESMA\_COMMENT\_DP\_EMIR\_CTs>

1. Please explain if you see a need for further clarification on how to identify OTC contracts for the purpose of the calculation of the positions to be compared to the clearing thresholds.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_1>

A substantial increase of the EMIR clearing threshold for commodities to an internationally comparable and more systemic relevant level (e.g., the USD 8 Billion threshold under the U.S. Dodd-Frank-Act), is necessary to facilitate the energy transition, enhance European competitiveness and improve market functioning, whilst safeguarding transparent and safe markets (cf. our response to Questions 6). For this purpose a change of the Level 2 text of EMIR would be required (Article 11 of Regulation (EU) No 149/2013) as any changes to ESMA’s QAs on EMIR implementation would not be sufficient to achieve these objectives.

At the same time, the scope of the EMIR CCT should be recalibrated to include activity that is relevant to the EU financial system.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_1>

1. Please explain if you see a need for further clarification to identify OTC contracts that can be considered as reducing risks directly relating to commercial activity or treasury financing activity. And please mention any additional aspects to be further considered with regards to the hedging exemption.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_2>

The existing EMIR definition of hedging is very similar to the definition in 3rd country jurisdictions such as the U.S. and it rightly includes portfolio- and macro hedging and hence its definition is not narrower than in comparable 3rd country regimes. However, we note that the substantially higher clearing threshold in those 3rd country jurisdictions (e.g., the USD 8 Billion threshold under the U.S. Dodd-Frank-Act), renders the limitations of the current hedging exemption less problematic. Therefore, we are requesting to keep at least the current Level 1 and 2 definitions of hedging in place and to keep this independent of any future review of the EMIR CCT.

However, the understanding of the term of underlying commercial business (“*commercial activity*”) in Art. 10 (3) of EMIR REFIT, which can be hedged through OTC derivatives transactions, should be clarified by ESMA through its EMIR QAs under the current Level 2 text of Article 10(1) of CDR 129/2013 to cover the following commercial activities:

* hedging the commercial risk of a first (non-hedging) derivative transaction – which forms part of the main commercial business of an NFC – with another second risk-reducing derivative transaction is currently not recognised as hedging, although economically the latter transaction can reduce the market price risk of the former and would form part of a normal economic hedging strategy (even though it would not be included under the definition of hedging under EMIR).
* Hence, the understanding of the term “commercial activity” could be clarified to cover the hedging of risks stemming from entering into financial instruments (commodity derivatives), when these financial instruments belong to the core commercial activity of an NFC-, e.g., those NFC-s whose core commercial activity is to deal in financial instruments as specialised energy and commodity trading firms do.
* the wording of the new ESMA EMIR QAs (OTC Question 10 (d), page 29, 31 – see [link](https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf)) that a core commercial activity of an NFC can consist of buying, selling or owning financial instruments.

This concerns the following cases:

* Where the OTC derivatives are used as part of the main commercial activity:

For example, if an energy trader or other energy firms enter into a financial Power Purchase Agreement (“PPA”), e.g., in the form of a financially settled swap fix-for-floating, with a renewable energy producer. The energy trader/firm are here providing an increasingly important role in facilitating and enabling renewable energy projects, for example, wind farms and hydrogen plants by providing these hedging transactions to the renewable producers.

Hence, these PPAs are used as a means of to underpin investment financing as it secures the renewable energy producer a fixed margin for its produced power quantities. The payments under such contracts depend not only on a price index, but also on the real physical production of a wind or solar farm by taking account the meter data of produced renewable energy (“pay as produced”). Therefore, these contracts share some characteristics of commercial power production and physical delivery activities.

These offtake structures qualify today as MiFID II financial instruments and therefore such activity is not deemed to constitute an eligible underlying commercial activity that could be hedged through OTC derivatives from the perspective of the energy trader. This narrow understanding of commercial activity is hence putting a real limitation to renewable energy business development.

The renewable energy industry would benefit from a clarification of the definition of underlying commercial activity to include financial instruments offered by NFCs as a risk management service to third parties for physical renewable energy project development.

* **Mitigation of commodity price risks:**

An energy trading firm might enter into a financial commodity derivative with another NFC to hedge its commodity price risk stemming from another commodity derivatives transaction previously entered into in the course of its core activity of energy trading. If that latter derivative does not hedge a corresponding commercial risk of the energy trading firm, that latter derivative is of a non-hedging nature, but still forms part of the core commercial activity of the concerned energy trading firm. In such a case the energy trading firm typically hedges the commodity price risk from the original derivative by entering into a further offsetting derivative which from an economical perspective is an effective hedge and thus objectively measurable as reducing the risk from the original derivative and thus should be classified as a hedge under the EMIR Level 2 rules.

<ESMA\_QUESTION\_DP\_EMIR\_CTs\_2>

1. Please provide information and examples on how counterparties count fungible ETDs and OTC derivatives for the purpose of the calculation of the clearing thresholds?

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_3>

TYPE YOUR TEXT HERE

**There are usually no fungible financial instruments for these hedging purposes that are traded on regulated markets as well as OTC.** This is for the following reasons:

* For example, the output of wind or solar parks depends on weather conditions, which can obviously change very quickly. Investors in these technologies face uncertainties about how much they will produce, when they will produce it and at what price. To manage these specific risks, they must be able to enter into tailor-made, bilaterally negotiated OTC hedging transactions with energy market participants. These transactions are usually not available at exchanges.
* Thus, managing these risks relies on the presence of firms in the OTC markets which are willing and able to provide tailor-made and structured risk management solutions in the form of transactions in OTC energy and commodity derivatives.
* For example, onshore and offshore wind generators enter into financially settled electricity swaps with particular price features to hedge their specific and complex market price risks. Such contracts cannot be found on regulated markets.
* In addition, even for more standardized risk profiles the contracts in the OTC trading markets are the only hedging possibility simply because the exchanges do not offer the long-term contracts needed to match the long-term commercial risks of the sustainable energy assets in question (such as wind or solar parks).
* Also, market participants do not use exchange products because the setup of an exchange access and the ongoing exchange and clearing processes are too resource intensive and particularly, exchange trading requires the provision of substantial liquidity funds to fulfil the huge variation and initial margin calls from CCPs.
* Finally, industrial consumers enter into long-term (10-20 years) power purchase agreements (“PPA”) with renewable power producers or re-sellers of such renewable production. Often such a PPA is structured as a bilaterally negotiated OTC cash settled fixed-for-floating swap, a so-called virtual PPA, which secures the renewable energy producer a fixed margin for its power quantities (hedging) and is combined with the delivery of the Guarantees of Origin (GoOs) to the industrial customer for his de-carbonization purposes. The reason is that for physical PPAs there are fewer potential counterparties and hence less liquidity as physical delivery requires the capability of both counterparties to handle physical deliveries.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_3>

1. Please provide data and arguments to illustrate the potential impact of the lack of an equivalence decision under Article 2a of EMIR and what could be done to alleviate your concerns (besides an equivalence decision)? Please specify the kind of transactions and activities that would be affected and the purpose of those, and whether there are alternatives.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_4>

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Recognition of LME and IFEU as equivalent by the EU is still the appropriate and targeted mitigant for this particular UK non-equivalence issue caused by Brexit.

The adverse impacts of the absence of an equivalence decision in respect of IFEU and LME under Article 2a of EMIR are caused by the regulatory fact that trades executed on these platforms will constitute over-the-counter (OTC) trades for the purposes of EMIR:

The consequence of this risk is that EU NFCs face a potential choice between meeting costly and burdensome NFC+-EMIR requirements or restricting their trading activities on UK exchanges to avoid breaching the EMIR CCT with the resulting impact and costs of becoming an NFC+ entity.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_4>

1. Please describe the scenarios when transactions do not qualify as hedging transactions.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_5>

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We refer to our response to Q2 above.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_5>

1. Please describe your views on how the EMIR framework works (also compared to other regimes) for the purpose of the clearing thresholds and the requirements triggered by those? Please provide examples and supporting data.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_6>

A substantial increase of the EMIR clearing threshold for commodities (“EMIR CCT”) to a more systemic level comparable with thresholds in 3rd country jurisdictions is urgently needed to facilitate the energy transition and enhance European competitiveness.

Therefore, ESMA and EU Commission should increase the EMIR CCT by way of a quick-fix amendment to Article 11 of Regulation (EU) No 149/2013.

The relatively small number of non-financial counterparties above the EMIR CCT (“NFC+s”) does not signify that this threshold is set at an appropriate level. It rather reflects the fact that staying below is the prevailing corporate strategy – involving curtailment of activity that would provide economic benefits across the EU – including greater market liquidity and efficiency.

**a) EU EMIR rules have the most restrictive approach of all the jurisdictions considered**

In general, we adhere to the main aims of EMIR to make derivatives markets more transparent, to mitigate credit risk and to reduce operational risks. However, as a result of the comparison between international standards of OTC derivatives markets regulation, the approach used by the EU under EMIR is the most restrictive of all approaches in a number of respects:

* Only the EU applies its regime to all trading activities around the globe without restriction, i.e., all world-wide energy and commodity derivatives activities count against EMIR’s clearing threshold, even if there is no EU-product, EU-venue or EU-entity involved;
* Only the EU includes any centrally cleared OTC derivatives as well as some physically settled exchange traded derivatives into the threshold calculation;
* Several jurisdictions, including Australia and Singapore, limit the application of OTC-clearing regulations solely to financial institutions
* Those jurisdictions which include non-financial market participants, including the U.S. and the EU, offer privileges for hedging transactions which are not considered for the clearing threshold.

**b) Potential adverse consequences for the energy transition**

The restrictive nature of the EU EMIR framework provides EU energy firms with limited headroom to offer suitable OTC hedging transactions to renewable energy producers in the EU and elsewhere in the world. This has direct adverse effects on the liquidity of OTC derivatives markets, the energy transition and European competitiveness.

In particular:

* for an energy firm providing hedges to renewable energy producers, these transactions will usually not be a hedge by itself and count against the EMIR clearing threshold.
* The consequence is that energy firms are incentivised to reduce the provision of these hedging activities to avoid the risk of breaching the current EMIR clearing threshold.
* Additionally, this will limit renewable energy producers’ entry into so-called virtual power purchase agreements (virtual PPAs) with industrial customers. These agreements are used as a means of investment financing as they secure the renewable energy producers a fixed margin for their power quantities (hedging) and are combined with the delivery of the Guarantees of Origin (GoOs) to the industrial customers for their de-carbonisation purposes.
* In addition, the volatility of market prices for power, EUAs and natural gas underlines the need for such long-term supply arrangements, secured and collateralized against market developments

**2. Broader issues of the EMIR framework**

Again, we request a quick fix increase to the EMIR CCT to address the urgent need to mitigate the adverse impacts on the energy transition and competitiveness of the EU markets as a more fundamental review of the EMIR Level 1 Text won’t be in place before 2026/27 (see our explanations above in the section “Introduction”).

In this context, we would like to raise the following broader issues with regard to the EMIR framework for NFC+ and of the EMIR CCT calculations, which emphasise the problems triggered by the low EMIR CCT.

The current EMIR framework exposes NFCs to the stark choice to either restrict or even stop their trading activities or to implement a very burdensome and costly NFC+ status; and

**Wide global scope of EMIR CCT calculations under Level 1 of EMIR:**

The extensive global reach of the EMIR CCT calculations for all in-scope instruments and activities – when compared to the scope of the 3rd country regime (see nr. 5 of benchmark table above) – puts EU NFCs at a substantial competitive disadvantage vis-à-vis their international competitors. The EU EMIR exposes EU energy firms to a substantial competitive disadvantage vis-à-vis firms from 3rd country jurisdictions because the latter are either not subject to the EU EMIR clearing rules or can make use of the more lenient OTC derivatives regime in their home jurisdictions. This is because under EMIR all world-wide energy and commodity derivatives activities count against the EMIR CCT, even if no EU-product, EU-venue or EU-entity is involved. This global nature of the EU-approach leads to much higher notional values since any OTC-derivative transaction of any non-EU group company concluded anywhere in the world contributes to the EU group’s clearing threshold consumption. For example, if a U.S. subsidiary of a European group enters into a financial swap with the aim to provide a hedge to an U.S. established Texas wind farm, the EU parent of this U.S. subsidiary must include this in its EMIR threshold calculations. Equally, an EU group is constrained by the EMIR clearing threshold to provide hedges to EU firms, while any 3rd country firm could compete without that limitation. ESMA’s EMIR QA, OTC Question 3 (d) (3) ) confirms this understanding.

As a result, not only is the €3bn EMIR CCT the lowest in international context, but it is also meant to cover all global entities of a group whereas the USD 8 Billion threshold under the U.S.-DFA, apart from being higher and only applying to financially settled products, requires a US-market-nexus of the activity (cf. nr. 5 of Benchmark Study Table in Section 1 above). Absent such, it is not considered for group aggregation.

On top, approaches taken in Australia and Singapore, allocate a substantially higher threshold (100 bn AUD in AUS) on **entity** level solely available for transactions booked in Australia.

* **Low, fixed EMIR CCT quickly consumed when energy and commodity prices rise:**

The EMIR CCT was defined in 2012 at a low fixed level of a gross notional value of 3bn (see Article 11 (e) CDR 149/2013). When compared to the prices in 2012, in 2021 the prices for gas, power and EUAs have increased considerably. This means that the gross notional value of open positions in OTC derivatives contracts relating to these commodities have substantially increased and, consequently, NFCs` positions in these quickly consume the fixed EMIR CCT. Hence, the headroom available in 2021 for NFCs to enter into new OTC derivative transactions is dramatically further reduced when compared to the date of setting the EMIR CCT in 2012.

* **Increased price volatility leads to high margin calls for cleared transactions resulting in difficult choices**

In the context of the above-mentioned price increases for power, gas and EUAs market participants face increased margin calls for cleared transactions and consequently face liquidity challenges and, hence, tough choices, which are emphasized by the low level of the EMIR CCT.

Energy firms active in the EU markets have turned to the EU’s Regulated Markets to hedge their natural long and short asset positions, for example, their power production.

As a result of the recent spike in volatility of commodity prices, energy firms have been subject to an unprecedented increase and stress in liquidity demands for covering both their initial and (if applicable) additional margin obligations for cleared derivatives on various CCPs.

**No ring-fencing of bilateral margining requirements under Level 1 of EMIR:**

The main impact of the NFC+ status is triggered by the bilateral margining obligation under Article 11 (3) of EMIR, in particular by the initial margining requirements. The bilateral margining requirements are by far the most burdensome and costly element of the EMIR obligations for NFC+s. Contrary to the ring-fencing of the clearing obligation under Article 10 (1) (c) of EMIR, the bilateral collateralizationof non-centrally-cleared OTC derivatives is not ring-fenced as it applies to all OTC derivatives asset classes across the entire corporate group.

**Need for equivalence decisions under Level 1 of EMIR for trading venues in 3rd countries:**

The need for an equivalence decision under Article 2a in conjunction with Article 2 (7) of EMIR considerably extends the population of global trading activities covered by the EMIR CCT calculation.

Other jurisdictions do not include derivatives traded on 3rd country venues in their threshold calculations.

In this context we consider that it is neither proportionate nor appropriate to have an equivalence regime purely for the purpose of establishing whether a derivative contract should be considered OTC or not for the purpose of the EMIR CCT calculations. We are concerned that the current lack of equivalence decisions is leading to unintended consequences for EU firms

* **EMIR CCT calculation methods embedded in Level 1 and 2 of EMIR:**

The current methodologies unduly inflate the gross notional values of OTC derivatives counting against the EMIR CCT.

**Restrictive netting under ESMA’s EMIR QA:**

Currently, for the purpose of the EMIR CTT calculation a very narrow understanding of netting is applicable (see ESMA QA (OTC Question 3 (f) ): Netting per contracts and counterparty should be understood as fully or partially offsetting contracts having exactly the same characteristics (type, underlying, maturity, etc.) with the only exception being the direction of the trade and notional amount (in case of partial offset) concluded with the same counterparty.

Other regulations applicable to energy commodity trading firms display a substantial wider understanding of netting, in particular for the ancillary activity tests under the CDR 2017/592.

**EMIR CCT calculation includes centrally cleared derivatives:**

EMIR CCT calculation includes OTC derivatives even if they are centrally cleared on EU CCPs or recognised 3rd country CCPs and hence in cases where the counterparty credit risk is fully mitigated.

**EMIR CCT calculation includes intragroup transactions:**

The EMIR CCT calculation under the Level 1 text of EMIR (Article 10 (3) ) includes intragroup transactions and this inflates the gross notional values of OTC derivatives counting against the EMIR CCT.

ESMA provides that if two NFCs belonging to the same group enter into an intragroup transaction with each other, which does not fall within the hedging definition, both sides of the transaction should be counted (ESMA EMIR QA, OTC Question 3 (d) (1)). The total contribution to the group-level threshold calculation would therefore be twice the notional amount of the contract.

**EMIR CCT calculations based on outstanding notional exposure under Level 1 text of EMIR:**

The calculation of the EMIR CCT under Article 10 (3) of EMIR is based on an outstanding notional exposure, i.e., shall be calculated by averaging the aggregated month-end outstanding notional values for the previous 12 months resulting from all relevant OTC derivatives contracts (ESMA EMIR QA, OTC Question 3 (a)). For example, the remaining outstanding notional exposure of a 10 year OTC swap counts during its entire duration against the EMIR CCT calculation.

Unlike under EMIR, under the U.S. DFA only swaps that have been entered into in the previous 12 months count against the threshold. Therefore, swaps entered into for a period of more than a year will drop out on a rolling basis

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_6>

1. Considering the current coverage provided by the clearing thresholds in relation to credit derivatives and the different type of counterparties (FCs and NFCs); is there any aspect or issue you consider ESMA should look into or pay attention to? Please, in your answer, provide as granular details and any relevant data to illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_7>

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<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_7>

1. Considering the current coverage provided by the clearing thresholds in relation to interest rate derivatives and the different type of counterparties (FCs and NFCs); is there any aspect or issue you consider ESMA should look into or pay attention to? Please, in your answer, provide as granular details and any relevant data to illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_8>

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<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_8>

1. Considering the current coverage provided by the clearing thresholds in relation to commodity derivatives and the different type of counterparties (FCs and NFCs); is there any aspect or issue you consider ESMA should look into or pay attention to? Please, in your answer, provide as granular details and any relevant data to illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_9>

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<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_9>

1. Considering the current coverage provided by the clearing thresholds in relation to equity derivatives and the different type of counterparties (FCs and NFCs); is there any aspect or issue you consider ESMA should look into or pay attention to? Please, in your answer, provide as granular details and any relevant data to illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_10>

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<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_10>

1. Considering the current coverage provided by the clearing thresholds in relation to currency derivatives and the different type of counterparties (FCs and NFCs); is there any aspect or issue you consider ESMA should look into or pay attention to? Please, in your answer, provide as granular details and any relevant data to illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_11>

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<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_11>

1. Beyond the different treatments between FCs and NFCs in the calculation, are there differences between the different types of counterparties that might justify a different calibration of the actual clearing thresholds? In addition, please consider if a different calibration of the current clearing thresholds by type of counterparty should apply in the same manner to all asset classes. Please provide any supporting data that might help illustrate your response.

<ESMA\_QUESTION\_ DP\_EMIR\_CTs\_12>

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**In line with advice by the Committee of European Banking Supervisors (“CEBS”), academic literature and current market data – that the current (by global standards, quite low) EMIR commodity clearing threshold of €3 billion can be increased to a substantially higher level without jeopardising the stability of the wider financial markets:**

* The size of the commodity derivatives markets is very small compared to other derivatives markets – Commodity derivatives account for only 1% of the outstanding notional value in 2020 (see ESMA Annual Statistics, Figure ASRD.4), while almost 80% come from interest rate derivatives. The stability of the financial sector (a key objective of EMIR) is therefore mainly dependent on asset classes other than commodities.
* NFCs account for the largest shares of counterparties in commodity derivatives – NFC accounted for 39% of the total notional amount in commodity derivatives in 2020 (see ESMA Annual Statistics, Figure ASRD.19). The level of the commodity clearing threshold therefore mainly affects the non-financial sector.
* NFCs active on the energy and commodity markets are not of systemic importance for the wider traditional financial markets. This view is supported by numerous independent analyses. For example, the Advice of the Committee of European Banking Supervisors (“CEBS”) of 10th October 2007 to the EU Commission (“CEBS-Advice”; page 2, ref. 12) clearly stated that *“… systemic risk concerns … appear significantly smaller relative to the systemic risks posed by banks and ISD financial investment firms. In the commodities case studies examined in this report, systemic concerns were limited and contained*.” ESMA seems to share this view in its consultation paper (see para. 157: *“[…] the absolute number of NFCs trading with commodity derivatives […] is lower than for other asset classes, which suggest NFCs are less significant from a systemic risk perspective.*”).

<ESMA\_QUESTION\_DP\_EMIR\_CTs\_12>

1. Looking at the simulations presented in the paper and at the impact they would have, do you have any views on the sensitivities of the thresholds?

<ESMA\_QUESTION\_DP\_EMIR\_CTs\_13>

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ESMA’s consultation paper (see Section 10) presents simulation results for variation of the current clearing thresholds (decrease by €0.5 billion and increase by €0.5 and €1.0 billion). ESMA intends to analyse the impact of a potential change in the clearing threshold on share of FCs and NFCs which are captured by the threshold.

We understand that ESMA conducts a *ceteris-paribus* calculation where it determines the shares of counterparties (notional value) below and above different levels of clearing thresholds based on the following observed trading data which is kept constant:

ESMA concludes that none of the variations of the commodity clearing threshold analysed in the consultation paper would have a material impact on the share of NFCs and notional value below or above the clearing threshold. This conclusion is flawed for several reasons:

* ESMA uses a static approach which takes the trading behaviour of NFCs (with the given low level of CCT at €3 billion) as given, and only varies the level of the clearing threshold. This type of analysis is misleading since the trading behaviour of NFCs is not exogenous to the level of the CCT and depends on the level of the clearing threshold itself:
  + NFC-s (98% of the companies) either have no significant derivative trading business or implement strict limits to avoid becoming NFC+.
  + Becoming an NFC+ is only commercially sensible if these companies exceed the threshold by a significant margin to compensate for the additional NFC+ costs.
* ESMA also does not present the results as curves, showing when and by how much a certain amount would actually affect NFCs. Instead, ESMA reports only results for three points on that curve.
* The simulations conducted by ESMA also do not consider important recent developments: ESMA utilizing only trading data for the year 2020, before the surge in commodity prices such as for CO2, gas and electricity. This means that the volumes (as measured in energy units rather than €bn) of commodity derivates tradable needed to stay below the clearing threshold would be significantly lower in 2021. If ESMA wants to analyse the impact of higher clearing thresholds, it needs to consider the effects of clearing thresholds on trading behaviour. For example, this could be captured in a like-for-like comparison with NFCs in other jurisdictions with higher thresholds (for example, the US, Singapore and Australia).

<ESMA\_QUESTION\_DP\_EMIR\_CTs\_13>