AUTORITÉ DES MARCHÉS FINANCIERS

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EMIR: entry into force of collateral requirements for non-centrally cleared derivatives on 4 February 2017

To mitigate the impact of a default by a market participant, the European Market Infrastructure Regulation (EMIR) requires that trading in derivatives be subject to central clearing or a bilateral exchange of collateral. Following the central clearing obligation, the margin exchange obligation is now taking effect.

On 15 December 2016, the Official Journal of the EU published the delegated regulation that defines and implements an obligation to exchange collateral for non-centrally cleared derivatives under the European Market Infrastructure Regulation (EMIR) on derivatives, central counterparties and trade repositories. To protect counterparties to a non-centrally cleared OTC derivative contract against the potential risk of default by the other counterparty, the regulation stipulates that the parties must make a bilateral exchange of initial and variation margins, and must specify both the methods used to calculate them, and the eligibility and diversification requirements that the collateral must meet.

Following the central clearing obligation, which took effect in 2016 for certain counterparties and whose scope will be gradually expanded through 2019, the obligation to exchange collateral for non-centrally cleared derivatives is the final stage of EMIR's implementation, which will be in full force from 2017.

Exchanging collateral

Each counterparty to an OTC derivative contract that is not centrally cleared faces the risk that the other counterparty will default before the final payment related to the transaction is made. Two types of collateral, in the form of an asset exchange, are necessary to properly manage this risk:

- the initial margin, which protects the counterparties against potential losses arising from future changes in the mark-to-market value of the contract during the time it takes to close out or replace the position in the event that the counterparty default;
- the variation margin, which protects counterparties against exposures related to the current market value of their OTC derivative contracts.

The collateral exchange requirements apply to financial entities dealing in derivatives and to non-financial firms whose derivatives positions exceed the clearing threshold. They apply to all OTC derivative contracts that are not centrally cleared.

They will progressively take effect starting in February 2017 according to the following schedule:

<table>
<tr><th>Types of counterparty</th><th>Initial margins</th><th>Variation margins</th></tr>
<tr><td>Counterparties belonging to a group whose positions exceed €3,000bn*</td><td>4 February 2017</td><td>4 February 2017</td></tr>
<tr><td>Counterparties belonging to a group whose positions exceed €2,250bn*</td><td>1 September 2017</td><td rowspan="5">1 March 2017</td></tr>
<tr><td>Counterparties belonging to a group whose positions exceed €1,500bn*</td><td>1 September 2018</td></tr>
<tr><td>Counterparties belonging to a group whose positions exceed €750bn*</td><td>1 September 2019</td></tr>
<tr><td>Counterparties belonging to a group whose positions exceed €8bn*</td><td>1 September 2020</td></tr>
<tr><td>Counterparties belonging to a group whose positions do not exceed €8bn*</td><td>Not applicable</td></tr>
</table>

** The positions to be compared with the thresholds correspond to the average of the gross notional amounts recorded on the last business day of March, April and May 2016 for all non-centrally cleared OTC derivative contracts, for all entities of the group. For funds, the calculation shall be made at the level of each fund.*

The obligation to exchange collateral in respect of single-stock equity options and index options will be phased in three years after the delegated regulation takes effect. Foreign exchange derivatives are also subject to specific treatment, with certain contracts exempt from the initial margin requirement and a phased-in enforcement of variation margin requirements.

Intragroup transactions are exempt from collateral requirements under certain conditions.

Read more

- Commission Delegated Regulation (EU) 2016/2251 of 4 October 2016 on risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty

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