

## European Market and Infrastructure Regulation (EMIR)



### Introduction

In August 2012, the 'European Market and Infrastructure Regulation' (EMIR) came into force as a binding law within the European Union, in order to try and increase the stability of Over-the-Counter (OTC) derivative transactions.

Counterparties who are subject to EMIR may be classified as follows:

- Financial Counterparties (FC); or
- Non-Financial Counterparties (NFC)

It is the responsibility of the counterparty to establish whether trading activities fall under the scope of EMIR and, if they do, to determine the counterparty classification.

### Implementation in Malta

During March 2013, the Minister of Finance, acting on the advice of the MFSA, amended the Financial Markets Act, to enable the EU wide EMIR regulation to be implemented in Malta.

From a practical point of view, implementation of EMIR in Malta targets 3 separate areas (i) Information and Guidance, (ii) Compilation of Data and (iii) Monitoring of Compliance.

EMIR concerns any person acting as a legal counterpart to a derivative contract.

### Financial Counterparties

The term "Financial Counterparties" refers to regulated entities, such as:

- financial or credit institutions
- investment firms
- UCITs, and where relevant, the management company
- AIFs, and where relevant their management company
- Insurance, assurance and reinsurance undertakings
- Institutions for occupational retirement provisions

In respect of FCs, EMIR states that all counterparties must report the details of any derivative contract to a registered trade repository within one working day of their conclusion, modification or termination. Trades outstanding on the 16th of August 2012 and still outstanding on the reporting start date are required to be reported within 90 days of the reporting start date. Trades outstanding on the 16th of August 2012 or entered into thereafter but not outstanding on the reporting start date should be reported within 3 years of the reporting start date. Therefore any derivative contract concluded after August 2012, and all subsequent modifications, need to be recorded, and such records maintained for at least 5 years following termination of the contract.

FCs are required to clear all OTC derivatives that will be included in the European Commission Regulatory Technical Standards (RTS), when entered into with counterparties that are either other FCs or NFCs, as detailed in the table on the following page.

**Table 1: EMIR Clearing Obligation Matrix**

Counterparty	FC	NFC+	NFC-
FC	✓	✓	X
NFC +	✓	✓	X
NFC-	X	X	X

If certain conditions are met, intragroup transactions may qualify for exemptions relating to the clearing obligation, and also in respect of exchange of collateral relating to the risk mitigation obligations. Pension scheme arrangements are also subject to exemptions with respect to the clearing obligation.

One of the requirements of EMIR is that of Risk Mitigation, which includes having certain procedures and arrangements in place in order to reduce the risks related to OTC derivative contracts which are not centrally cleared. The procedures required by EMIR are:

- Timely confirmation of trades by the required deadline
- An agreement on how portfolios are to be reconciled
- An agreed procedure to identify and resolve conflicts which may arise between the parties
- A process to regularly analyse the possibility of conducting portfolio compression
- A procedure for the accurate and appropriate segregated exchange of collateral
- Mark-to-Market (or Mark-to-Model) value of outstanding contracts

### Non-Financial Counterparties

The term “Non-Financial Counterparties” refers to all undertakings that trade derivatives that are not classified as FCs, Trade Repositories and Central Counterparties. EMIR further subdivides NFCs into NFC+ and NFC- depending on the value of non-hedging derivatives entered into by the NFC. The distinction is based on the following criteria:

- Over €1bn, individually, of credit derivatives and equities derivatives
- Over €3bn, individually, of interest rate derivatives, foreign exchange derivatives and commodity derivatives and other derivatives (in gross notional value)

NFCs in excess of this clearing threshold for any class of derivatives are deemed to be NFC+, while those below are considered to be NFC-. NFCs exceeding the clearing threshold are required to clear OTC derivative contracts that are subject to the clearing obligation, explained in Table 1 above.

NFCs are required to report all derivative contracts to a trade depository. EMIR states that all counterparties must report the details of any derivative contract to a registered trade repository within one working day of their conclusion, modification or termination. Trades entered into by NFCs prior to the 16th August 2012 and which were still outstanding as at that date, as well as trades entered into on the 16th August 2012 or thereafter, also need to be reported. However, the reporting obligation will not come into play prior to 14 February 2014.

As in the case of FCs, EMIR requires that certain procedures and arrangements are put in place for NFCs in order to reduce the risks related to OTC derivative contracts which are not centrally cleared. The procedures required by EMIR are:

- Timely confirmation of trades by the required deadline
- An agreement on how portfolios are to be reconciled
- An agreed procedure to identify and resolve conflicts which may arise between the parties
- A process to regularly analyse the possibility of conducting portfolio compression

If the obligations and provisions of EMIR are not adhered to, the MFSA may impose an administrative penalty not exceeding €150,000.

KPMG may help you ensure you are prepared for EMIR.

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