



European regulators respond to the international postponement of the implementation of the bilateral margin requirements under EMIR

In response to the COVID-19 outbreak the European Supervisory Authorities (EBA, EIOPA and ESMA - the ESAs) published, on 4 May 2020, their 'Final Report EMIR RTS on various amendments to the bilateral margin requirements in view of the international framework' ([RTS](#)), to amend the Delegated Regulation on the risk mitigation techniques for non-centrally cleared OTC derivatives (bilateral margining), under the European Markets Infrastructure Regulation (EMIR), to incorporate a one-year deferral of the two final implementation phases of the bilateral margining requirements.

The ESAs have intensified their coordination with national competent authorities (NCAs), as well as with relevant authorities from other jurisdictions in order to ensure adequate regulatory actions where needed during this crisis. In this context, these amending draft RTS were developed to further facilitate an internationally coordinated approach on how to adapt the implementation of the bilateral margin requirements.

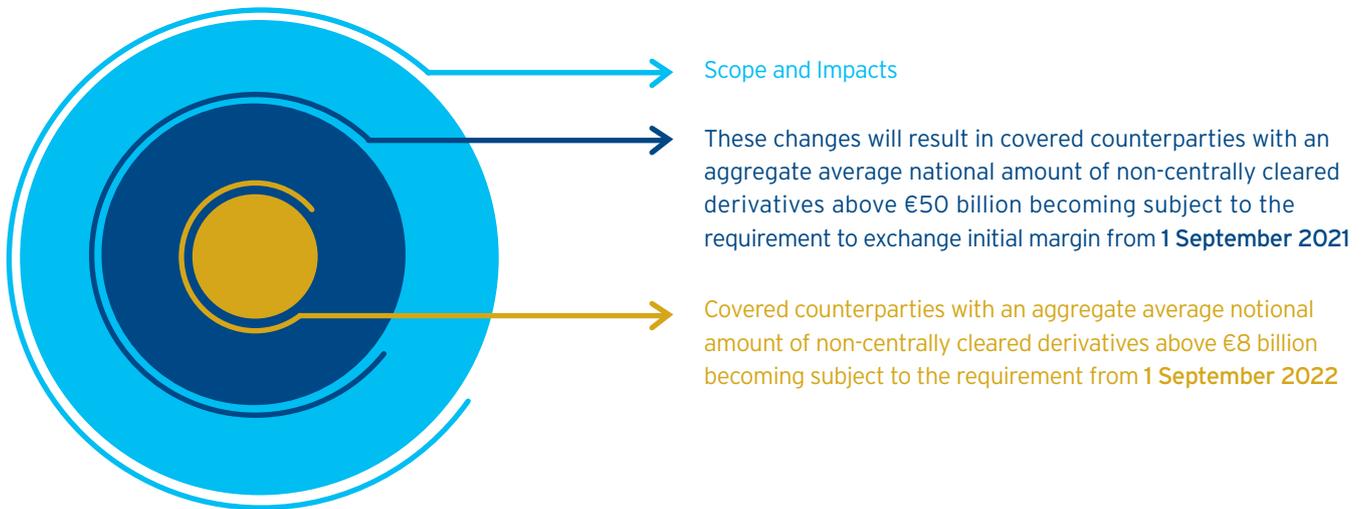
[The international approach](#)

The new draft RTS propose to introduce a number of amendments to the Commission Delegated Regulation on

bilateral margining that take into account the international framework already agreed by the Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO).

In order to provide additional operational capacity for counterparties to respond to the immediate impact of COVID-19, the draft RTS present the changes to the Delegated Regulation on bilateral margining to incorporate in to the EU regulatory framework the one-year deferral agreed by the BCBS and IOSCO.

The ESAs have developed the RTS under Article 11(15) of EMIR.



Operational perspective

From a process point of view, the amendments introduced in the draft RTS are of a proportionate nature. They are also in line with the international framework and take into account the status of the implementation of this framework at the international level which has also been documented and analysed.

In addition, some of the deadlines were fast approaching at the time of the first submission of this Final Report in December 2019, and have since past. In particular the deferred date of application for intragroup transactions as well as for equity options, which was 4 January 2020.

The ESAs feel that market participants would benefit from knowing as early as possible how to prepare for these requirements. Finally, many of these requirements have also been called for by a large range of market participants.

Document layout

Section I: Explains the background to the ESA proposals;

Section II: Details the rationales for the RTS amendments; and

Section III: Outlines the ESAs' proposal.

Key to note

No further amendment of the framework, except for the deferral introduced in response to the COVID-19 outbreak,

and more specifically no further extension of the phase-in and no change of the thresholds, in particular the 8 billion threshold, are envisaged.

As a result, it is important that the counterparties who have been facing some challenges in their preparation for complying with the initial margin requirements and that under the proposed draft RTS would have some additional time to complete them, continue their preparation efforts in order to be able to comply by the deadline.

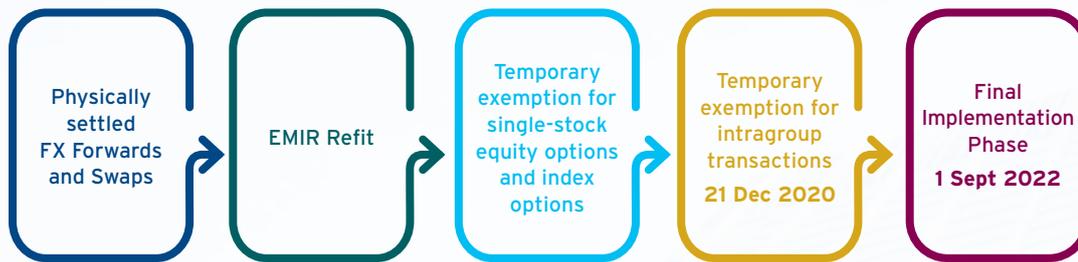
Next steps

The Final Report has been sent to the European Commission, and the ESAs are submitting the draft technical standards presented in the Annex for endorsement in the form of a Commission Delegated Regulation.

Following the endorsement, they will then be subject to non-objection by the European Parliament and the Council.

The ESAs cannot disapply EU law, so in view of the remaining steps that the draft RTS need to go through before being finalised and entering into force, and in light of some of the relevant deadlines¹, the ESAs expect competent authorities to apply the EU framework in a risk-based and proportionate manner until the amended RTS enter into force.

¹ With regards to the bilateral margin requirements and the treatment of physically settled FX forward and swap contracts, intragroup contracts, equity option contracts and the implementation of the last phase of the initial margin requirements as proposed in the draft RTS.



Looking at the EMIR RTS in more detail

As mentioned in our summary above, in response to the COVID-19 outbreak, the Final Report has been updated to take into account the related decision from the BCBS and IOSCO communicated on 3 April 2020 to defer the implementation of the remaining phases of the initial margin requirements.

In terms of substance, the resulting targeted update of the Final Report centres around the introduction of a new section 2.2.2 B and the related change to the draft RTS with respect to the applicable deadlines.

This updated version of the Final Report on the draft RTS on bilateral margining thus replaces entirely the version submitted to the Commission in December 2019.

BCBS and IOSCO had already agreed to extend the deadline for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives by one year.

The purpose of the international-level extension was to provide additional operational capacity for firms to respond to the immediate impact of COVID-19 and, at the same time, facilitate covered entities to act diligently to comply with the requirements by the revised deadline.

With this extension, the final implementation phase will take place on **1 September 2022**.

Following on from this, the ESAs have reviewed the application of the relevant requirements of Commission Delegated Regulation (EU) No 2016/2251 on bilateral margining and the amending draft RTS submitted in December 2019, and have identified the amendments necessary in order to extend the implementation deadlines by one year for those counterparties in the final two phases.

Physically settled FX Forwards and Swaps

BCBS and IOSCO agree that standards apply for variation margin to be exchanged on physically settled FX forwards and swaps in a manner consistent with the final policy framework and that those variation margin standards are implemented either by way of supervisory guidance or national regulation.

The international standards state that variation margining of physically settled FX forwards and swaps is both an established practice among significant market participants and a prudent risk management tool that limits the build-up of systemic risk, and thus that variation margining should apply to these contracts.

The international standards recommend implementing this requirement by way of national regulation or supervisory guidance. The EU initially implemented these international standards by way of regulation², including a deferred date of application for physically settled FX forwards until 3 January 2018, which was the date of application of the revised Markets in Financial Instruments Directive (MiFID II) and thus when the definition of physically settled FX forwards was further harmonised.

²Specifically, this was done through Article 27(a) of Commission Delegated Regulation on bilateral margining, which exempts these contracts from the exchange of initial margin, in line with the international framework, and through Article 37(2) thereof for the variation margin requirements.



Although the bilateral margin requirements for physically settled FX forwards were meant to apply from the entry into force of MiFID II at the start of January 2018, market participants raised some concerns which the ESAs analysed.

Based on the material presented to the ESAs, it became apparent that the adoption of the international standards in other jurisdictions via supervisory guidance had led to an international scope of application that is more limited than the scope the ESAs had proposed in the RTS (and which was finally embedded in the EU rules). Whereas the requirement remains relevant for transactions between institutions, the implementation appeared to pose a challenge regarding transactions between institutions and end-users.

Following from this, the ESAs developed and submitted in December 2017 a joint RTS on bilateral margining with respect to physically settled FX forward contracts, which proposed a permanent exemption for certain contracts when entered into between institutions and end-users.

The process for the proposed amending RTS from December 2017 has not been completed and so has not become law. However, the ESAs are of the view that the rationale for the proposed amendment is still valid.

EMIR Refit

More recently, following the EMIR Review, the co-legislators agreed on a range of amendments to EMIR in Regulation (EU) 2019/834, also referred to as the EMIR Refit text. The EMIR Refit text was published on 28 May 2019 and entered into force on 17 June 2019.

It is important to note in this context that the co-legislators have reiterated through the EMIR Refit text the importance of international consistency in the implementation of the international standards on bilateral margining, and in particular with regards to the treatment of physically settled FX forwards and swaps. Recital 21 of the EMIR Refit text makes clear that there is a need for international regulatory convergence.

Following from this, the ESAs have discussed with the European Commission the need to replace the amendment submitted by the ESAs in December 2017 by a new amendment covering a broader scope, i.e. not only covering physically settled FX forwards, but covering both physically settled FX forwards and swaps, with the same exemption for both. The draft RTS included in the Annex contains this broader scope.

Temporary exemption for single-stock equity options and index options

The Commission Delegated Regulation on bilateral margining contains a range of implementation timelines, including a phase-in for the initial margin requirements as well as deferred dates of application for certain contracts and counterparties. In particular, the requirements for single-stock equity options or index options transactions were deferred until 4 January 2020.

Three years later, the situation has not materially changed. Certain jurisdictions have not implemented these requirements for these contracts or have also introduced temporary exemptions in the meantime. The ESAs reiterate the view that, from a prudential point of view, the international framework agreed on by all the participant authorities in the BCBS and IOSCO discussions is a crucial pillar in ensuring safer derivatives markets, limiting the counterparty risk between counterparties trading derivatives, and thus that its coordinated implementation is key in reaching this objective.

With the view to continue monitoring regulatory developments in other jurisdictions and ensuring that appropriate requirements are in place in the European Union to mitigate counterparty credit risk in respect of such contracts whilst avoiding scope for regulatory arbitrage, it would thus appear proportionate to extend by one year the current deferred application of the margin requirements for single-stock equity options or index options transactions in the EU framework. The draft RTS included in Annex contains this proposed amendment.



Temporary exemption for intragroup transactions

Another deferred date of application of the bilateral margin requirements relates to intragroup transactions with a third country entity in the absence of an equivalence decision adopted by the European Commission pursuant to Article 13(2) of EMIR. The requirements for these intragroup transactions were deferred until 4 January 2020.

The rationale for the exemption from the clearing obligation is the same as for the exemption from the bilateral margin requirements, i.e. broadly speaking that those deferred dates were necessary to ensure that such intragroup OTC derivative contracts were not subject to the EMIR clearing or bilateral margin requirements before the adoption of the relevant equivalence decisions. The ESAs are thus of the view that in light of this common rationale for a temporary exemption, it is proportionate to also extend the temporary exemption for bilateral margin and to align it with the exemption for the clearing obligation, i.e. until 21 December 2020. The draft RTS included in the Annex contains this proposed amendment.

Link to the Final Report can be found [here](#)

Please contact for further details:

David Morrison

Global Head of Trustee and Fiduciary Services
david.m.morrison@citi.com
 +44 (0) 20 7500 8021

Ann-Marie Roddie

Head of Product Development Fiduciary Services
annmarie.rodzie@citi.com
 +44 (1534) 60-8201

Amanda Hale

Head of Regulatory Services
amanda.jayne.hale@citi.com
 +44 (0)20 7508 0178

Caroline Chan

APAC Head of Fiduciary Business
caroline.mary.chan@citi.com
 +852 5181 2602

Shane Baily

EMEA Head of Trustee and Fiduciary Services
 UK, Ireland and Luxembourg
shane.baily@citi.com
 +353 (1) 622 6297

Jan-Olov Nord

EMEA Head of Fiduciary Services
 Netherlands and Sweden
janolov.nord@citi.com
 +31 20 651 4313

www.citibank.com/mss

The market, service, or other information is provided in this communication solely for your information and "AS IS" and "AS AVAILABLE", without any representation or warranty as to accuracy, adequacy, completeness, timeliness or fitness for particular purpose. The user bears full responsibility for all use of such information. Citi may provide updates as further information becomes publicly available but will not be responsible for doing so. The terms, conditions and descriptions that appear are subject to change; provided, however, Citi has no responsibility for updating or correcting any information provided in this communication. No member of the Citi organization shall have any liability to any person receiving this communication for the quality, accuracy, timeliness or availability of any information contained in this communication or for any person's use of or reliance on any of the information, including any loss to such person.

This communication is not intended to constitute legal, regulatory, tax, investment, accounting, financial or other advice by any member of the Citi organization. This communication should not be used or relied upon by any person for the purpose of making any legal, regulatory, tax, investment, accounting, financial or other decision or to provide advice on such matters to any other person. Recipients of this communication should obtain guidance and/or advice, based on their own particular circumstances, from their own legal, tax or other appropriate advisor.

Not all products and services that may be described in this communication are available in all geographic areas or to all persons. Your eligibility for particular products and services is subject to final determination by Citigroup and/or its affiliates.

The entitled recipient of this communication may make the provided information available to its employees or employees of its affiliates for internal use only but may not reproduce, modify, disclose, or distribute such information to any third parties (including any customers, prospective customers or vendors) or commercially exploit it without Citi's express written consent. Unauthorized use of the provided information or misuse of any information is strictly prohibited.

Among Citi's affiliates, (i) Citibank, N.A., London Branch, is regulated by Office of the Comptroller of the Currency (USA), authorised by the Prudential Regulation Authority and subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority (together, the "UK Regulator") and has its registered office at Citigroup Centre, Canada Square, London E14 5LB and (ii) Citibank Europe plc, is regulated by the Central Bank of Ireland, the European Central Bank and has its registered office at 1 North Wall Quay, Dublin 1, Ireland. This communication is directed at persons (i) who have been or can be classified by Citi as eligible counterparties or professional clients in line with the rules of the UK Regulator, (ii) who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 and (iii) other persons to whom it may otherwise lawfully be communicated. No other person should act on the contents or access the products or transactions discussed in this communication. In particular, this communication is not intended for retail clients and Citi will not make such products or transactions available to retail clients. The information provided in this communication may relate to matters that are (i) not regulated by the UK Regulator and/or (ii) not subject to the protections of the United Kingdom's Financial Services and Markets Act 2000 and/or the United Kingdom's Financial Services Compensation Scheme.

© 2020 Citibank, N.A. and/or each applicable affiliate. All rights reserved by Citibank, N.A. and/or each applicable affiliate. Citi and Arc Design is a trademark and service mark of Citigroup Inc., used and registered throughout the world.

GRA31519 05/20

