

## Non-financial counterparties subject to EMIR

This factsheet is for non-financial counterparties (NFCs) calculating the clearing threshold and complying with the EU Regulation on derivatives, central counterparties and trade repositories (EMIR) and which are a part of a group with entities that are Financial Counterparties (FCs).

### **Our review**

Following the original review we conducted to understand how NFCs are defining their hedging activity and monitoring their status against the clearing threshold, we extended it to include NFCs which are part of a group with entities that are FCs. Between September and November 2013, we also discussed the challenges of complying with EMIR.

This information is important to NFCs which are a part of an FC group. This is because any NFC entering into positions in over-the-counter (OTC) derivatives contracts that exceed the clearing thresholds specified by ESMA under article 11 of the OTC derivative technical standards has been required to notify its competent authority under Article 10(1) of EMIR since 15 March 2013.

We generally observed the following findings from our recent discussions with NFCs which are part of a group with FCs. In some cases these mirror the findings from our original review to understand how NFCs are defining their hedging activity and monitoring their status against the clearing threshold (<http://www.fca.org.uk/your-fca/documents/non-financial-counterparties-factsheet>), but here are some additional observations.

### **What did our review find?**

#### ***NFCs accurately classifying hedging and non-hedging transactions***

- NFCs had established a clear trading strategy statement identifying the NFC's hedging needs, with trading activity monitored against the strategy and any trades not directly related to the hedging part of the strategy clearly identified.
- Where NFCs have some trading which is hedging and some which is designed to be profitable for the firm without a link back to commercial or treasury risk, NFCs clearly flagged the non-hedging trades in internal systems and counted them towards the clearing threshold calculation.
- NFCs operated an asset-backed trading strategy to hedge future revenue, with the aim of demonstrating that trading activity is objectively necessary for 'hedging

purposes' and does not amount to speculative activity. We note this was achieved by ensuring the derivative contract does not exceed the hedging need as this would otherwise be classified as a speculative trade.

***Additional points from the review of NFCs which are a part of a group with FCs***

- NFCs are largely using derivatives to hedge their commercial and treasury risks rather than participating in the derivatives market for speculative trades which other parts of the group, in particular, FCs may be engaged in.
- The FC part of the group generally provides treasury services including derivatives execution through asset backed trading to the NFC.
- The NFC population within a group with FCs is commonly represented by a central team within the group which is responsible for identifying NFCs within the group, and ensuring those NFCs meet the requirements as stated by EMIR. Where the activities of NFCs within the group are not centrally monitored their activities need to be adequately identified and monitored to be included in the global group clearing threshold calculation.
- The NFC population is usually represented by a single point of contact responsible for reporting against the clearing threshold to the FC part of the group, usually the group treasury, which takes the global group position into account. NFCs were largely governed by a group policy for defining hedging trades, with a process in place to monitor the level of non-hedging activity if trading is outside of this scope.

***Points that NFCs delegating EMIR obligations to FCs within their group should consider to comply with EMIR***

- The group treasury of an FC generally acted as a centre of expertise and knowledge on EMIR, providing support to NFCs within the group to meet their requirements. Often NFCs delegated the EMIR clearing threshold calculation, risk mitigation requirements and reporting to the FC group treasury. Where this was the case, some groups had not always adequately considered any conflicts of interest which could arise where the FC is the main or only counterparty to the NFC.
- Most groups had recognised that where an NFC has delegated responsibility for performance of certain EMIR requirements, the relevant NFC entities retain responsibility for compliance and need to have the ability to monitor activities that have been undertaken on their behalf and had decided to use contractual agreements to support this position.
- NFCs had begun to consider the reporting requirements, but those that are a part of a group with FCs were relying on an FC within the group to perform reporting on behalf of the NFC. Most groups were aware that even where trades undertaken by NFCs within a group with FCs are always back-to-back contracts with other FCs within the group, the back-to-back contracts need to be reported, and were already planning to include NFCs in their system for reporting intra-group derivative contracts.