

EUROPEAN MARKET INFRASTRUCTURE REGULATION

EMIR: Q&A



REGULATION EMIR

SUMMARY

Three new “early stage” obligations in force since 15 March:

1. Timely confirmation of new OTC derivatives transactions for all counterparties
2. Non-financial counterparty notification to regulatory authorities depending on the size of the derivatives book
3. Mark-to-market valuations of non-cleared OTC derivatives

Topics

- **Non-financial counterparties:** “NFC”, “NFC+” and clearing thresholds (pp1-2)
 - **ISDA’s NFC Representation Protocol** (p3)
 - **Timely confirmations:** impact on trading relationships and contractual documentation (pp3-4)
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 - **Portfolio Reconciliation and Dispute Resolution:** our obligations, new ISDA protocol (p5)
- **Capital Requirements Directive, Product exemptions:** (p5)

Contact

If you wish to discuss further, please contact the BNP Paribas Fortis European Regulatory Reforms team (Regreform.be@bnpparibasfortis.com) or your Fixed Income Sales Representative.

The European Regulation on OTC Derivatives, Central Counterparties and Trade Repositories came into force on 16 August 2012 (also known as the [European Market Infrastructure Regulation](#) or “EMIR”); however, many of its key provisions are being phased in over the course of 2013 and 2014. With the publication of certain [EMIR Regulatory Technical Standards](#) (“RTS”) on 23 February 2013, a number of early stage obligations began applying to non-financial counterparties on 15 March 2013.

This FAQ has been prepared by BNP Paribas Fortis to provide you with some basic information about the key issues that will impact our trading relationship and to keep you informed about our preparation for complying with EMIR as and when the relevant obligations take effect during the course of 2013 and beyond.

1. Which obligations came into force on 15 March 2013?

Three key new “early stage” obligations came into force on Friday, 15 March:

- a. The obligation on all financial and non-financial counterparties to obtain timely confirmation of new OTC derivatives transactions. There are no exceptions to this requirement for EU financial and non-financial counterparties within the scope of EMIR.
- b. The obligation that non-financial counterparties established in the European Union will need to notify their national competent authorities and the European Securities and Markets Authority (ESMA) if and when they cross the clearing threshold.
- c. The obligation that all financial counterparties and non-financial counterparties (which have crossed the clearing threshold) must begin, if they are not already doing so, conducting daily mark-to-market valuations of their non-cleared OTC derivative transactions.

Furthermore, we at BNP Paribas Fortis must classify all our derivatives counterparties for EMIR purposes because, for example, the time we will have to obtain timely confirmation will depend on how our counterparties are classified.



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NFC/NFC+ STATUS

2. We have been informed that we may need to make notifications to regulatory authorities in certain circumstances. Is this correct?

This is correct for EU-established non-financial counterparties. Under EMIR, a non-financial counterparty (“NFC”) is required to notify its relevant national competent authority (assuming a competent authority has been designated, as required by EMIR) and ESMA from 15 March 2013 if, on any given day, the aggregate gross notional value of the positions in “non-hedging” OTC derivatives of that NFC and all other NFCs in its group exceeds any one of the following asset-specific clearing thresholds:

- €1 billion for credit derivatives;
- €1 billion for equity derivatives;
- €3 billion for interest rate derivatives;
- €3 billion for FX derivatives, and
- €3 billion for commodity and other derivatives

In fact, there are a number of notifications that are required. ESMA have confirmed in an [FAQ published on 20 March 2013](#) that NFCs should have started calculating whether or not they have exceeded any of the specified thresholds from 15 March 2013 and that a notification must be sent to the relevant national competent authority and ESMA “only on the first day” that they exceed any of the clearing thresholds.

An NFC will become an NFC+ if the rolling average position over 30 working days exceeds any of the clearing thresholds. We understand from ESMA’s FAQ that a second notification is not required here. In other words, the required notification only applies upon the relevant clearing threshold being exceeded on any given day and should not be based on the rolling average positions over 30 working days. However, as ESMA confirms in its FAQ, a second notification will be required “as soon as possible” to the relevant national competent authority and ESMA when the average position over 30 working days no longer exceeds any of the clearing thresholds.

As you may be aware, [ESMA](#) and a number of national competent authorities (for example, the AMF, the FSA and BaFin) have published specimen notification forms and further information about the notification process. ESMA’s FAQ also includes guidance about NFC group notifications. We recommend that you contact your external professional advisers if you have any questions about the notification process, for example, what you should do if the relevant national competent authority has not yet published prescribed notification forms.

3. Will BNP Paribas Fortis tell us if we are an NFC or NFC+? If not, how should we go about determining our status under EMIR?

EMIR imposes the obligation on NFCs to determine their own status and this has recently been reconfirmed by ESMA in its FAQ. As set out above, it is your responsibility to notify the relevant national competent authority and ESMA when you exceed the relevant clearing threshold. Although you do not have a regulatory obligation to notify us, it is important that BNP Paribas Fortis is notified about your status as quickly as possible, simply because your status under EMIR determines the obligations that apply to the derivatives trading relationship between us.

BNP Paribas Fortis will seek to obtain clarification as to your NFC or NFC+ status under EMIR. We can obtain this information from you, for example, via the ISDA 2013 EMIR NFC Representation Protocol (please

see question 5 below) or alternatively you can choose to notify us directly without adhering to an industry standard Protocol. We may also contact you directly to ask you to confirm your status. However, BNP Paribas Fortis will not be under any obligation to conduct any verification of any information received from you as to your status under EMIR and we will rely on such information unless we are in possession of other data which clearly demonstrates that information you have given in this regard is incorrect.

In order to determine your status under EMIR, you will need to consider the definitions of a financial counterparty and non-financial counterparty under EMIR. In broad terms, a financial counterparty is an authorised or regulated bank, investment firm, insurance, reinsurance or assurance undertaking, an alternative investment fund managed by alternative investment fund managers, a UCITS or pension fund. If you are not a financial counterparty as defined under EMIR, by default you will be an NFC if you are an undertaking established in the European Union. You will then need to determine if you are simply an NFC or, more importantly, an NFC+, by undertaking the clearing threshold assessment that we refer to in our response to question 2 above.

4. In calculating whether or not our positions are over the relevant clearing threshold, we understand that we can ignore commercial hedges. Is this correct?

This is correct. In determining whether or not your OTC derivatives positions exceed the relevant clearing threshold, the calculation will exclude OTC derivatives contracts “which are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity”.

A few important points to note:

- a. OTC derivatives positions must be calculated on a group wide basis, i.e. the calculation must be performed on an aggregate basis across all the OTC derivatives positions entered into by all the NFCs within your group even if there are group NFCs that are established outside the European Union
- b. The RTS set out in detail the criteria for establishing which OTC derivative contracts will be risk reducing – only one of the criteria in the RTS needs to be satisfied for the hedging exemption to be available; thus, if you determine that the OTC derivatives contracts you enter into qualify for hedge accounting treatment under IFRS, those contracts will qualify for the hedging exemption
- c. If one of the relevant clearing thresholds is exceeded, you will be required to clear (as and when the mandatory clearing obligation comes into effect) all clearing eligible hedging transactions, irrespective of whether they are for hedging purposes across all five asset classes.
- d. If one NFC in the group is an NFC+, all other NFCs in the group engaging in derivatives business will be deemed to be NFC+s
- e. In its 20 March 2013 FAQ, ESMA stated that OTC derivatives contracts which are “cleared on a voluntary basis” must be included in the calculation of the clearing threshold. In other words, both voluntarily cleared and non-cleared bilateral OTC derivatives contracts are caught.

ESMA also consider that derivative contracts traded on multilateral trading facilities (“MTFs”) are OTC derivatives under EMIR, and that derivative contracts executed on non-EU exchanges that are equivalent to an EU-regulated market in accordance with the relevant provisions of MiFiD can be excluded from the clearing threshold determination, but not derivatives traded in other non-EU exchanges



(i.e., those non-EU exchanges that are not equivalent to a regulated market). Unfortunately, to date there is no publicly available list of non-EU exchanges equivalent to a regulated market. It is not yet clear how NFCs are expected to factor this into their clearing threshold determinations.

5. ISDA recently published a NFC Representation Protocol. Is BNP Paribas Fortis expecting all its corporate clients to adhere to this Protocol? Does it make a difference if we are not established in the European Union?

On 8 March 2013, ISDA published the [ISDA March 2013 EMIR NFC Representation Protocol](#) (the "NFC Protocol"). The NFC Protocol is designed to help all market participants amend multiple ISDA Master Agreements to incorporate representations relating to each party's NFC status. The NFC Protocol is an "evergreen" protocol in the sense that it remains open for adherence until ISDA designates a closing date and it is open to non-ISDA members as well as ISDA members (such as BNP Paribas Fortis). BNP Paribas Fortis will be adhering to the NFC Protocol as a non-representing financial counterparty and will be the recipient (alongside the other financial counterparties that adhere and with whom you have derivatives trading relationships)

of the representations. BNP Paribas Fortis will seek to obtain certain representations from you confirming your NFC or NFC+ status under EMIR and for the most part we will attempt to do so via this Protocol.

The NFC Protocol is also open to NFCs established outside the European Union and we would encourage all clients with whom we have ISDA Master Agreements to adhere to this Protocol. Please note that an adhering party is required to pay a one-time fee of US \$500 to ISDA upon or before submitting its adherence letter. ISDA have produced an FAQ explaining [how the NFC Protocol works](#).

Not all our clients will have executed ISDA Master Agreements with us; indeed, a number of our clients will have executed domestic OTC derivatives Master Agreements (developed by local trade and industry associations) with us. Some clients may not choose to adhere to the NFC Protocol or the local equivalent, if any, and instead choose to notify BNP Paribas Fortis bilaterally. As set out in our response to question 3 above, the key requirement is that you inform us about your status irrespective of whether this is via an industry Protocol or a bilateral notification to us.

TIMELY CONFIRMATION

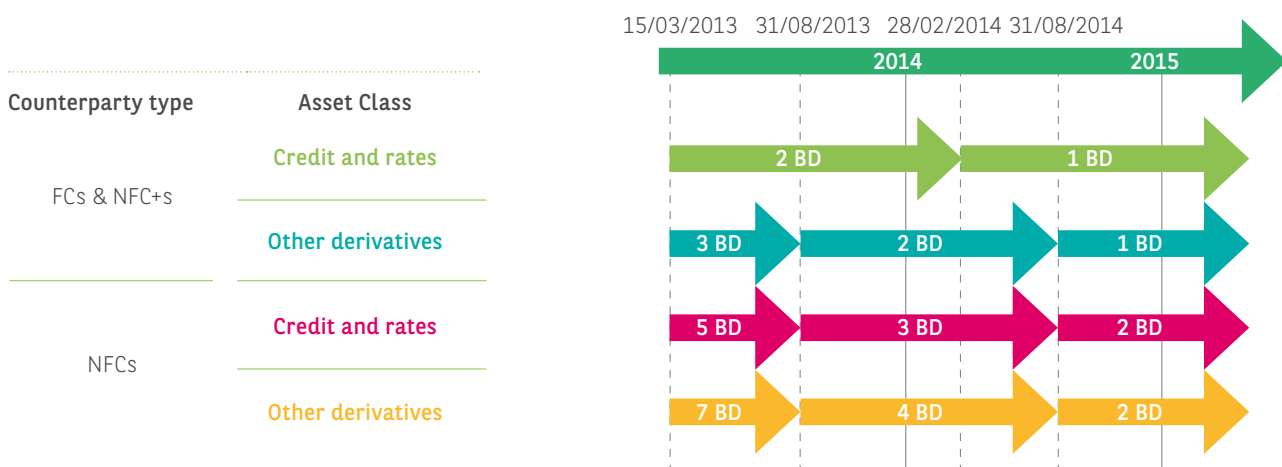
6. How will the requirement to obtain "timely confirmation" of our derivatives transactions impact on our trading relationship with BNP Paribas Fortis?

The answer to this question depends largely upon your status under EMIR, hence the importance of (a) determining whether you are an NFC or NFC+ and (b) notifying the relevant competent authority and ESMA, and BNP Paribas Fortis, as soon as possible. It also depends on the nature of the OTC derivatives transactions which we trade together and the time at which those transactions are entered into. As a general comment, trades with NFCs will be subject to slightly longer time frames.

As a reminder, the RTS define a confirmation as "the documentation of the agreement of the counterparties to all the terms of an over-the-counter (OTC) derivative contract".

Please note that the timely confirmation requirements only apply to non-cleared bilateral OTC derivatives transactions. Exchange-traded derivatives transactions, such as futures, are not within scope.

The following table sets out clearly the different permutations for timely confirmation in business days (BD) under the RTS:



In each case, transacting after 4pm local time or with a counterparty located in a different time zone "which does not allow confirmation by the set deadline" (e.g. the United Arab Emirates during Eid) results in the confirmation having to take place as soon as possible and, at the latest,



one business day following the relevant confirmation deadline set out above.

The RTS require us to have procedures and arrangements in place that will allow us to confirm non-cleared OTC derivatives within the timelines set out above. In its [8 February 2013 FAQ](#), the European Commission confirmed that the confirmation deadlines are not hard deadlines to be complied with case-by-case and that the timely confirmation obligation is focused on market participants having appropriate procedures and arrangements in place in order to achieve the relevant deadlines. According to the Commission's FAQ, if a financial counterparty or a NFC has appropriate procedures and arrangements in place but nevertheless does not achieve the deadlines for "legitimate reasons", this will have to be reported to its relevant national competent authority. The relevant competent authority will be able to examine those procedures and arrangements and determine whether or not sufficient efforts have been made to achieve the deadlines.

Whilst an NFC or NFC+ established in the European Union will be directly caught by EMIR (when trading derivatives), the early-stage obligations in EMIR will not apply directly to an NFC or NFC+ established outside the European Union. However, as a financial counterparty under EMIR, BNP Paribas Fortis has to put the necessary procedures and arrangements in place to ensure timely confirmation with respect to the OTC derivatives trades with all its counterparties irrespective of their location in the European Union or outside of it. BNP Paribas Fortis has a regulatory obligation under EMIR to report to our competent authority on a monthly basis the number of trades, for which the confirmation has not been agreed, that remain outstanding for more than 5 business days after trade execution.

7. Will the timely confirmation requirements have an impact on the contractual documentation BNP Paribas Fortis has in place with its clients?

On 8 March 2013, ISDA published the [Timely Confirmation Amendment Agreement](#) ("**Amendment Agreement**"), which is a form of agreement that market participants can use as part of their tool kit for compliance with the timely confirmation requirements. The Amendment Agreement is to be implemented bilaterally with counterparties (and not via a protocol). In short, this sets out standard provisions addressing:

- a. which party/parties will deliver a non-electronically matched confirmation (given the short timeframes under EMIR/RTS to agree confirmations); and
- b. "deemed acceptance" language

However, it does not set out consequences for any breach of the provisions. The Amendment Agreement will require bilateral negotiation with each applicable counterparty, and this will be both time- and resource-consuming. Furthermore, BNP Paribas Fortis considers that EMIR will be directly binding on EU entities subject to its provisions irrespective of whether or not they sign an Amendment Agreement; in other words, execution of the Amendment Agreement is superfluous. Therefore, BNP Paribas Fortis is not proposing to execute the Amendment Agreement with NFC/NFC+ established in the European Union.

The general regulatory direction and objective is towards the confirmation of as many OTC derivatives transactions as possible by electronic means, where available. BNP Paribas Fortis is committed

to this objective. However, where confirmation by electronic means is not possible, BNP Paribas Fortis will still use other forms of confirmation (e.g. fax or manually-processed emails, as recognised by ESMA in their FAQ) provided that we are comfortable that we can comply with the timely confirmation requirements (which in turn requires engagement from our counterparty). As set out above in our response to question 6, these confirmation deadlines are ambitious and encourage electronic confirmation and standardisation of the documentation. ESMA has also confirmed that negative affirmation is acceptable, where agreed between the parties.

DAILY VALUATION

8. If we are an NFC+, do we now need to undertake daily mark-to-market valuations of our derivatives positions?

Yes. The requirement to undertake mark-to-market valuations on a daily basis is one of the risk mitigation obligations in EMIR. Where market conditions prevent marking-to-market, reliable and prudent marking-to-models must be used. The RTS set out the criteria for using marking-to-model. This obligation is imposed on financial counterparties and NFC+s and the mark-to-market requirement is a requirement to value on a daily basis the value of all outstanding non-cleared OTC derivatives contracts.

TRADE REPORTING

9. Will BNP Paribas Fortis report trades on our behalf when the trade reporting obligations under EMIR take effect?

BNP Paribas Fortis will be able to offer to report new OTC derivatives trades entered into with BNP Paribas Fortis (or a BNP Paribas Fortis affiliate company) on your behalf. Our preferred trade repository is DTCC, in part due to the range of product reporting offered through DTCC's global trade repository service. A dedicated communication on BNP Paribas Fortis EMIR Trade Reporting services is available.

PORTFOLIO RECONCILIATION AND DISPUTE RESOLUTION

10. What are our obligations?

From 15 September 2013, counterparties are obliged to have agreed procedures and processes for reconciling their portfolios (including key trade terms), either directly or via one or more third parties (such as TriOptima), and resolving any disputes in relation to their contracts, covering (amongst other things) the valuation of contracts, the exchange of collateral, etc. Parties are required to agree specific processes for the escalation of disputes that are not resolved in five business days.

It is important that these procedures and processes are agreed as soon as possible. On a strict reading of the Regulation, these processes and arrangements would need to be in place before we trade. It is also clear that compliance with these obligations is going to be monitored closely by competent authorities; in particular, we (and other financial counterparties) are obliged to report to regulators on those disputes of more than €15m that are outstanding for more than 15 business days. Note that other risk mitigation obligations may apply. A dedicated communication on these risk mitigation obligations and their impact on BNP Paribas Fortis' derivatives trading relationship with its clients is available.



11. Is ISDA preparing another protocol to help counterparties comply with their EMIR Portfolio Reconciliation and Dispute Resolution obligations?

Yes, an ISDA protocol is ready and covers Portfolio Reconciliation and Dispute Resolution obligations under EMIR. It also includes a confidentiality waiver linked to the trade reporting obligation. We strongly encourage our clients to sign this protocol, once published, as a basis for agreeing more detailed procedures on portfolio reconciliation and dispute resolution.

12. Not all counterparties have executed ISDA Master Agreements with BNP Paribas Fortis. Are other industry bodies developing a protocol-type approach or alternative documentation to address Portfolio Reconciliation and Dispute Resolution?

We understand that both the French and German Banking associations (who publish the respective local law documentation for derivatives contracts) are developing their own documentation. Please note, however, that the final ISDA protocol referred to under Q11 above is likely to be sufficiently broad to cover relationships in relation to non-cleared OTC Derivatives which are not governed by an ISDA Master Agreement so that it will be possible for parties to seek to satisfy their obligations, (for example, in respect of transactions entered into under the FBF Master Agreement) by adherence to the ISDA Protocol.

In tandem with this, please note that ISDA has also published a "reporting protocol" which contains a global confidentiality waiver to help facilitate the reporting of transactions in compliance with the various different regulatory regimes (e.g. EMIR, DFA, Hong Kong law, Singapore law, etc.) that may apply to any given derivatives trade.

WHAT ELSE?

13. In the revised draft of the Capital Requirements Directive, reference is made to a number of EMIR definitions and classifications. Is this correct?

This is correct, although in some cases this has been used to create helpful exemptions rather than extend the scope of a given measure. For example, the definitions of non-financial counterparties and derivatives in EMIR have been utilised in the recently-agreed fourth iteration of the Capital Requirements Directive (or "CRD IV") impacting European entities. In particular, there is an express carve-out

from the proposed capital charge on Credit Valuation Adjustments ("CVA") for non-cleared derivatives transactions with those non-financial counterparties that are below the clearing threshold (on the threshold generally, see Q2 above).

PRODUCT EXEMPTIONS

14. Are FX spot and forward transactions within the scope of EMIR?

Spot products are generally exempted from all EMIR obligations on the grounds that they are not "derivatives" for the purposes of the Regulation. Regarding FX forwards, although the general market consensus is that they are caught within the scope of the "derivatives" definition for the purposes of EMIR, there is express wording in the recitals of EMIR recognising that certain types of FX derivatives and covered bond derivatives may not be suitable for mandatory clearing or bilateral collateralisation. ESMA will take a view on which OTC derivatives should be excluded when it makes its clearing eligibility determination and when it publishes its regulatory technical standards on bilateral collateralisation for non-cleared OTC derivatives following the final report of the BCBS-IOSCO (in the Autumn 2013). Such derivatives would however be subject to other EMIR requirements (e.g. trade reporting).

MISCELLANEOUS

15. Are there any other consequences on BNP Paribas Fortis' trading relationship with its clients?

Other than the issues we have addressed in this FAQ, there should be no other immediate consequences on our trading relationship. However, your status as an NFC or NFC+ will continue to have knock-on consequences for the other EMIR obligations which will come into force later, notably the mandatory clearing and the collateralisation of non-cleared trades. We shall endeavour to inform you in good time about any changes to our relationship resulting from EMIR obligations.



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