

## E-ALERT | FINANCIAL SERVICES AND REGULATION

February 5, 2014

### EMIR: THE REPORTING OBLIGATION APPLIES FROM 12 FEBRUARY 2014

The European Market Infrastructure Regulation (EMIR) entered into force on 16 August 2012<sup>1</sup>. In addition to rules for central counterparties (CCPs) and trade repositories (TRs), EMIR sets out three principal requirements for counterparties to derivative contracts:

- **Clearing:** Financial counterparties (FCs) and non-financial counterparties (NFCs) that exceed a clearing threshold must clear OTC derivative contracts *subject to the clearing* obligation pursuant to Article 4 of EMIR;
- **Reporting:** All counterparties (FCs and NFCs) and CCPs must report the conclusion, modification and termination of *all* derivative contracts to a trade repository (TR) pursuant to Article 9 of EMIR; and
- **Risk Mitigation:** Pursuant to Article 11 of EMIR, counterparties must adopt risk mitigation techniques for *uncleared* OTC derivative contracts, including timely confirmation (all counterparties), portfolio reconciliation (all counterparties), margining uncleared OTC contracts (FCs and NFCs exceeding a clearing threshold only) and additional regulatory capital requirements (FCs only).

The reporting obligation comes into force on **12 February 2014**, and this note sets out what the obligation entails and what affected entities need to be doing to prepare.

#### I. SCOPE OF THE REPORTING OBLIGATION

The purpose of the obligation is to provide a central store of information on risk in relation to the OTC derivatives markets, which the European Securities and Markets Authority (ESMA) and certain central banks may access. It extends to **all derivative contracts**, whether admitted to trading on a trading venue or traded bilaterally<sup>2</sup>, as well as exchange-traded derivative contracts admitted to trading on a non-EU market or platform. EMIR uses the definition of derivatives found in the Markets in Financial Instruments Directive (MiFID). However, FX spot transactions are not covered, and the Financial Conduct Authority (FCA) in the United Kingdom has provided guidance that FX forwards will not be within scope either. This may not be so in other EEA jurisdictions.

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<sup>1</sup> Regulation (EU) 648/2012 on OTC derivatives, central counterparties and trade repositories, OJ L 201, 27.7.2012.

<sup>2</sup> On December 20, ESMA published its updated Questions and Answers on EMIR (the "ESMA Q&As") with new specific guidance for reporting of exchange-traded derivatives (ETD). The [ESMA Q&As](#) advise that the reporting obligation applies to all counterparties to an ETD transaction and that client, broker, clearing member and CCP must submit reports. However, the reporting obligation does not apply where the broker executes such transaction on behalf of a client because, in such cases, the broker is not considered a counterparty to the transaction.

The reporting obligation applies to **all CCPs and counterparties**, including FCs, NFC+s and NFC-s. While CCPs and counterparties may delegate<sup>3</sup> the reporting obligation to a third party, they remain liable for timely and accurate reporting by the third party.

All types of counterparty to a transaction have an obligation to make a report, though one party may report on behalf of both by prior arrangement. However, counterparties and CCPs must also ensure that details of their derivative contracts are reported without duplication *i.e.*, that there is only one report produced by each counterparty (or on their behalf) for each trade that they carry out. This excludes subsequent modifications to a report. In the scenario where the CCP and counterparties use different TRs, or submit separate reports on the same trades, they should ensure that they report with consistent data, including the same trade ID and the same valuation information.

Where the derivatives contract is entered into between an EEA entity and a non-EEA entity, the EEA entity will have the obligation to report. It must state in the report that the other party is non-EEA. Intra-group trades should also be reported, and specified as such in the report. However, if the transaction is carried out between two branches of the same legal entity, no report is required.

The International Swaps & Derivatives Association (ISDA) and the Futures and Options Association (FOA) published a model reporting delegation agreement, which is available at the following [link](#). Broadly, this is designed to help parties meet their reporting obligations under EMIR through the use of a standard form contract, which both parties can use to delegate their reporting obligations to a specialised entity offering reporting services.

## II. TIMING OF REPORTS

Where clearing takes place on the same day as execution, reports should be submitted to a TR up to one working day after the execution. Where clearing takes place after the day of execution and after reporting is made, this should be reported as an amendment to the original report up to one day after the clearing took place.

## III. BACKLOADING

The reporting obligation applies to previous derivative contracts as follows:

- Contracts entered into on or after 16 August 2012 (*i.e.*, the date of entry into force of EMIR) and outstanding on 12 February 2014 must be reported on **12 February 2014**.
- Contracts entered into before 16 August 2012 and outstanding on both 16 August 2012 and 12 February 2014 must be reported within **90 days** of 12 February 2014.
- Contracts entered into before 16 August 2012 and outstanding on 16 August 2012 but not outstanding on 12 February 2014, or entered into on or after 16 August 2012 and not outstanding on 12 February 2014 must be reported within **three years** of 12 February 2014.

As explained above, derivative contracts entered into, modified, or terminated on or after 12 February 2014 must be reported by the next working day.

## IV. CONTENT OF REPORTS

The regulatory technical standards (RTS)<sup>4</sup> with regard to reporting specify that counterparties must report:

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<sup>3</sup> The FCA considers that the delegation of reporting under EMIR is subject to the SYSC 8 (Outsourcing) requirements of the FCA Handbook.

- (a) details relating to each of the counterparties to the derivative contract (“Counterparty Data”); and
- (b) details pertaining to the derivative contract concluded between the two counterparties (the “Common Data”), which must be agreed between the two counterparties.

All FCs and NFC+s must additionally include information on exposures, such as mark-to-market or mark-to-model valuations in reports.

The RTS specify 26 Counterparty Data fields and 59 Common Data fields for each trade report. While many of these data fields are self-explanatory, some rely on new standards and systems under development. These include the legal entity identifier (LEI) a unique 20 digit alphanumerical code that may be used for eight of the 26 Counterparty Data fields. LEIs remain under development and are not yet widely available. However, a number of data providers have been authorised by the Financial Stability Board to provide so-called “pre-LEIs”.<sup>5</sup>

Moreover, while Article 4 of the RTS states that a derivative contract shall be identified using a “unique product identifier” subject to eight criteria that have been endorsed by ESMA for reporting purposes, ESMA has not endorsed any product identifiers to date. As a result, counterparties and CCPs may identify a derivative contract by:

- (a) combining the assigned ISO 6166 ISIN code or Alternative Instrument Identifier with the corresponding ISO 10962 Classification of Financial Instruments code, or
- (b) using an interim taxonomy set out in Article 4 of the RTS, which identifies derivative contracts by class and type.

## V. RECORD KEEPING

Counterparties shall keep a record of any derivative contract they have concluded and any modification for at least five years following the termination of the contract.

## VI. REMEDIES FOR BREACHES

EMIR sets out the framework for penalties imposed on counterparties that breach the EMIR obligations, including the reporting obligation<sup>6</sup>. Specific sanctions and penalties must be determined by individual Member States, but should include at least administrative fines. The FCA’s rules on breaches of EMIR in the FCA Handbook specify a wide range of fines and include possible public censures. A number of Member States have yet to finalise their frameworks for breaches of EMIR. The full list of notifications may be found [here](#).

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<sup>4</sup> Commission Delegated Regulation (EU) No 148/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards on the minimum details of the data to be reported to trade repositories, OJ L 52, 23.2.2013, p. 1–10.

<sup>5</sup> Pre-LEIs can be issued by any of the endorsed pre-LOUs (Local Operating Units) of the Global Legal Entity Identifier System. The list of endorsed pre-LOUs is available at: [http://www.lei.org/publications/gls/lou\\_20131003\\_2.pdf](http://www.lei.org/publications/gls/lou_20131003_2.pdf)

<sup>6</sup> Article 12, EMIR

## VII. PREPARATION FOR FIRMS

### A. Reporting

Firms which need to comply with the reporting obligation must ensure that they have obtained an LEI, as well as know their own counterparty classification. They should also find out the classification status of their counterparty to the trade.

### B. Systems

They should review their systems and procedures to ensure that transactions can be reported, and that specific people are in charge of collating and transmitting reports to TRs within the legal time limits. Firms should be making arrangements with regard to who is reporting the transaction. Are they doing this themselves or will they delegate it? They will need to have the relevant agreements in place.

### C. Documentation

Contracts may require agreed changes before they can be reported to TRs (in relation to data privacy and confidentiality). The protocols provided by ISDA and FOA may be used to simplify this process.

### D. TRs

Firms must register and connect with one of the TRs which has been approved by ESMA. There are currently six.<sup>7</sup> Following this, firms must also arrange to backload historical data to the TR.

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<sup>7</sup> The current list of registered TRs may be found [here](#).