



Brussels, 13.6.2016  
C(2016) 3544 final

**COMMISSION DELEGATED REGULATION (EU) .../...**

**of 13.6.2016**

**supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards on the direct, substantial and foreseeable effect of derivative contracts within the Union and the prevention of the evasion of rules and obligations**

(Text with EEA relevance)

## **EXPLANATORY MEMORANDUM**

### **1. CONTEXT OF THE DELEGATED ACT**

The Markets in Financial Instruments Regulation (Regulation (EU) No 600/2014, MiFIR) sets out a formal regulatory procedure for mandating trading in derivatives that have been considered to be clearing-eligible and which are sufficiently liquid to take place on a range of trading venues. MiFIR also determines that the trading obligation shall apply to third-country entities, that would be subject to the clearing obligation if they were established in the Union, which enter into derivative transactions pertaining to a class of derivatives that has been declared subject to the trading obligation, provided that the contract has a direct, substantial and foreseeable effect within the Union or where such obligation is necessary or appropriate to prevent the evasion of any provision of this Regulation.

In this context, Article 28(5) of MiFIR requires the European Securities and Markets Authority (ESMA) to develop draft regulatory technical standards to establish when a third country counterparty should be subject to the trading obligation mandated by Article 28 of MiFIR.

The draft regulatory technical standards were submitted to the Commission on 28 September 2015. In accordance with Article 10(1) of Regulation No (EU) 1095/2010 establishing the ESMA, the Commission shall decide within three months of receipt of the draft standards whether to endorse them. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

### **2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT**

In accordance with Article 10 of the Regulation (EU) 1095/2010 ESMA has carried out a public consultation on the draft regulatory technical standards. A consultation paper was published on 19 December 2014 on ESMA website and the consultation closed on 2 March 2015. In addition, the ESMA sought the views of the Securities and Markets Stakeholder Group (SMSG) established in accordance with Article 37 of the ESMA Regulation. The SMSG chose not to provide advice on these issues due to the technical nature of the standards.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1095/2010, the ESMA has submitted its impact assessment, including the analysis of costs and benefits related to the draft technical standards. This analysis is available at [http://www.esma.europa.eu/system/files/2015-esma-1464\\_annex\\_ii\\_-\\_cba\\_-\\_draft\\_rts\\_and\\_its\\_on\\_mifid\\_ii\\_and\\_mifir.pdf](http://www.esma.europa.eu/system/files/2015-esma-1464_annex_ii_-_cba_-_draft_rts_and_its_on_mifid_ii_and_mifir.pdf).

### **3. LEGAL ELEMENTS OF THE DELEGATED ACT**

These RTS specify the types of contracts with third country counterparties that are subject to the trading obligation, as well as the cases where the trading obligation is necessary and appropriate to prevent avoidance of the provisions in MiFIR. These RTS, where possible and appropriate, should be identical to the one adopted under Article 4(4) of EMIR which specifies the types of contracts with third country counterparties that are subject to the clearing obligation as well as the cases where the clearing obligation is necessary and appropriate.

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(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012<sup>1</sup>, and in particular Article 28(5) thereof,

Whereas:

- (1) Given the broad variety of over-the-counter (OTC) derivative contracts, in order to determine when an OTC derivative contract may be considered to have a direct, substantial and foreseeable effect within the Union as set out in Article 28(2) of Regulation (EU) No 600/2014 and to specify cases where it is necessary or appropriate to prevent the evasion of rules and obligations arising from any provision of Regulation (EU) No 648/2012 of the European Parliament and the Council<sup>2</sup>, a criteria-based approach should be adopted.
- (2) Article 33(3) of Regulation (EU) No 600/2014 states that the conditions laid down in Articles 28 and 29 of that Regulation are deemed to be fulfilled when at least one of the counterparties is established in a country for which the Commission has adopted an implementing act declaring equivalence in accordance with Article 33(2) of Regulation (EU) No 600/2014. The present regulatory technical standards should therefore also apply to contracts where both counterparties are established in a third country whose legal, supervisory and enforcement arrangements have not yet been declared equivalent to the requirements laid down in that Regulation.
- (3) Certain information on contracts concluded by third country entities would still only be available to third country competent authorities. Therefore Union competent authorities should closely cooperate with those third country competent authorities in order to ensure that the relevant provisions are applied and enforced.
- (4) Given the intrinsic relationship between this Regulation and Commission Delegated Regulation (EU) No 285/2014<sup>3</sup>, the technical terms necessary for a comprehensive understanding of the technical standards should have the same meaning.

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<sup>1</sup> OJ L 173, 12.6.2014, p. 84.

<sup>2</sup> Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

<sup>3</sup> Commission Delegated Regulation (EU) No 285/2014 of 13 February 2014 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical

- (5) OTC derivative contracts concluded by entities established in third countries covered by a guarantee provided by entities established in the Union create a financial risk for the guarantor established in the Union. Given that the risk would depend on the size of the guarantee granted by financial counterparties in order to cover OTC derivative contracts and given the interconnections between financial counterparties compared to non-financial counterparties, only OTC derivative contracts concluded by entities established in third countries that are covered by a guarantee which exceeds certain quantitative thresholds and is provided by financial counterparties established in the Union should be considered as having a direct, substantial and foreseeable effect in the Union.
- (6) Financial counterparties established in third countries can enter into OTC derivative contracts through their Union branches. Given the impact of the activity of those branches on the Union market, OTC derivative contracts concluded between those Union branches should be considered to have a direct, substantial and foreseeable effect within the Union.
- (7) OTC derivative contracts that are entered into by specific counterparties with the primary purpose of avoiding the application of the clearing obligation or of the risk mitigation techniques applicable to entities that would have been the natural counterparties to the contract, should be considered as evading the rules and obligations laid down in Regulation (EU) No 600/2014 as they hinder the achievement of one of the purposes of that Regulation, namely mitigating counterparty credit risk.
- (8) OTC derivative contracts that are part of an arrangement whose characteristics are not supported by a business rationale or commercial substance and have as their primary purpose the circumvention of the application of Regulation (EU) No 600/2014, including rules relating to the conditions of an exemption, should be considered as evading the rules and obligations laid down in that Regulation.
- (9) Situations where the individual components of the arrangement are inconsistent with the legal substance of the arrangement as a whole, where the arrangement is carried out in a manner which would not ordinarily be used in what is expected to be reasonable business conduct, where the arrangement or series of arrangements includes elements that have the effect of offsetting or nullifying their reciprocal economic substance, where transactions are circular in nature, should be considered as indicators of an artificial arrangement or an artificial series of arrangements.
- (10) Given that third country entities affected by these regulatory technical standards require time in order to arrange for compliance with the requirements of Regulation (EU) No 600/2014 when their OTC derivative contracts fulfil the conditions set out in these regulatory technical standards for being considered to have a direct, substantial and foreseeable effect within the Union, it is appropriate to delay the application of the provision containing those conditions by six months.
- (11) For reasons of consistency and in order to ensure the smooth functioning of the financial markets, it is necessary that the provisions laid down in this Regulation and the provisions laid down in Regulation (EU) No 600/2014 apply from the same date.
- (12) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority (ESMA) to the Commission.

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standards on direct, substantial and foreseeable effect of contracts within the Union and to prevent the evasion of rules and obligations (OJ L 85, 21.3.2014, p. 1).

- (13) ESMA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council<sup>4</sup>,

HAS ADOPTED THIS REGULATION:

*Article 1*  
**Definitions**

For the purposes of this Regulation the following definition shall apply:

‘guarantee’ means an explicitly documented legal obligation by a guarantor to cover payments of the amounts due or that may become due pursuant to the OTC derivative contracts covered by that guarantee and entered into by the guaranteed entity in favour of the beneficiary where there is a default as defined in the guarantee or where no payment has been effected by the guaranteed entity.

*Article 2*  
**Contracts with a direct, substantial and foreseeable effect within the Union**

1. An OTC derivative contract shall be considered as having a direct, substantial and foreseeable effect within the Union when at least one third country entity benefits from a guarantee provided by a financial counterparty established in the Union which covers all or part of its liability resulting from that OTC derivative contract, to the extent that the guarantee meets both following conditions:
  - (a) it covers the entire liability of a third country entity resulting from one or more OTC derivative contracts for an aggregated notional amount of at least EUR 8 billion or the equivalent amount in the relevant foreign currency, or it covers only a part of the liability of a third country entity resulting from one or more OTC derivative contracts for an aggregated notional amount of at least EUR 8 billion or the equivalent amount in the relevant foreign currency divided by the percentage of the liability covered;
  - (b) it is at least equal to 5 per cent of the sum of current exposures, as defined in Article 272(17) of Regulation (EU) No 575/2013 of the European Parliament and of the Council<sup>5</sup>, in OTC derivative contracts of the financial counterparty established in the Union issuing the guarantee.
2. When the guarantee is issued for a maximum amount which is below the threshold set out in paragraph 1(a), the contracts covered by that guarantee shall not be considered to have a direct, substantial and foreseeable effect within the Union unless the amount of the guarantee is increased, in which case the direct, substantial and foreseeable effect of the contracts within the Union shall be re-assessed by the

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<sup>4</sup> Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

<sup>5</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

guarantor against the conditions set out in points (a) and (b) of paragraph 1 on the day of the increase.

3. Where the liability resulting from one or more OTC derivative contracts is below the threshold set out in paragraph 1(a), such contracts shall not be considered to have a direct, substantial and foreseeable effect within the Union even where the maximum amount of the guarantee covering such liability is equal to or above the threshold set out in paragraph 1(a) and even where the condition set out in paragraph 1(b) has been met.
4. In the event of an increase in the liability resulting from the OTC derivative contracts or of a decrease of the current exposure, the guarantor shall re-assess whether the conditions set out in paragraph 1 are met. Such assessment shall be done respectively on the day of the increase of liability for the condition set out in paragraph 1(a), and on a monthly basis for the condition set out in paragraph 1(b).
5. OTC derivative contracts for an aggregate notional amount of at least EUR 8 billion or the equivalent amount in the relevant foreign currency concluded before a guarantee is issued or increased, and subsequently covered by a guarantee that meets the conditions set out in paragraph 1, shall be considered as having a direct, substantial and foreseeable effect within the Union.
6. An OTC derivative contract shall be considered as having a direct, substantial and foreseeable effect within the Union where the two entities established in a third country enter into the OTC derivative contract through their branches in the Union and would qualify as financial counterparties if they were established in the Union.

### *Article 3*

#### **Cases where it is necessary or appropriate to prevent the evasion of rules or obligations provided for in Regulation (EU) No 600/2014**

1. An OTC derivative contract shall be deemed to have been designed to circumvent the application of any provision of Regulation (EU) No 600/2014 if the way in which that contract has been concluded is considered, when viewed as a whole and having regard to all the circumstances, to have as its primary purpose the avoidance of the application of any provision of that Regulation.
2. For the purposes of paragraph 1, a contract shall be considered as having for primary purpose the avoidance of the application of any provision of Regulation (EU) No 600/2014 if the primary purpose of an arrangement or series of arrangements related to the OTC derivative contract is to defeat the object, spirit and purpose of any provision of Regulation (EU) No 600/2014 that would otherwise apply including when it is part of an artificial arrangement or artificial series of arrangements.
3. An arrangement that intrinsically lacks business rationale, commercial substance or relevant economic justification and consists of any contract, transaction, scheme, action, operation, agreement, grant, understanding, promise, undertaking or event shall be considered an artificial arrangement. The arrangement may comprise more than one step or part.

*Article 4*

**Entry into force and application**

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

This Regulation shall apply from the date referred to in the second paragraph of Article 55 of Regulation (EU) No 600/2014.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 13.6.2016

*For the Commission  
The President  
Jean-Claude JUNCKER*