EMIR: Q&A

12th November 2013

Hello, and welcome to the EMIR Regulation Question and Answer Session.

Our speakers today are:

- **Aline De Leener,** Fixed Income Trading Business Manager, Co-ordinating EMIR implementation for Fixed Income
- **Nicolas Mehta,** Head of Derivatives Policy and Development within CIB Legal, covering EMIR Legal implementation and documentation

The following Q&A session reflects BNP Paribas' views on the topics addressed, but we must stress that this does not constitute legal or regulatory advice and we recommend you address legal or regulatory concerns to your own advisors.

Introduction

As a European bank, BNP Paribas is subject to the European Regulation on OTC Derivatives, Central Counterparties and Trade Repositories (commonly known as the European Market Infrastructure Regulation or "EMIR"), which came into force on 16 August 2012. The main provisions in EMIR are being phased in over the course of 2013 and 2014, with some key obligations that came into force on 15th September 2013.

Whilst, absent special circumstances, the regulation should not apply directly to our counterparties outside the European Union, it places certain requirements on us as regards derivatives transactions that we may trade with you. Many of these requirements were designed with clients' best interests in mind, by seeking to improve the stability of the derivatives markets, encourage robust processes for the confirmation and reconciliation of trades, minimise the risk of disputes in relation to the terms of agreed trades and ensure that, where disputes do arise, that they are resolved promptly.

If you deal in over-the-counter ("OTC") derivatives with BNP Paribas (including our overseas branches) or one of our other European group entities, then we will need your assistance to comply with EMIR in respect of OTC derivatives transactions that we enter into with you.

The definition of OTC derivatives in EMIR refers to all derivatives contracts which are not "executed on a regulated market" or an equivalent third country market. As a result, all derivatives contracts executed by other means (such as single and multi-dealer portals offering B2C trade execution facilities), are considered as OTC derivative contracts under EMIR.

In most cases, you can assist us in meeting these obligations in part by adhering to the two EMIR protocols published by ISDA in relation to the implementation of EMIR. Which will be discussed in more detail later.

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Regulation | **EMIR**

Further information

If you wish to discuss further, please contact the BNP Paribas European Regulatory Reforms team (Regreform.eu@uk.bnpparibas.com) or your BNP Paribas Relationship Manager or Sales Representative.

This will not make you directly subject to EMIR, but will help us meet our regulatory obligations in respect of the transactions we enter into with you. Adhering to the protocols should also ensure that you get the benefit of the new provisions without having to agree separate bilateral documentation with us. We may also require your assistance in respect of certain operational matters e.g. in relation to the timely confirmation of your transactions and the reconciliation of your portfolios with us. We mention specific timing requirements in this regard, below.

Scope

1. What is EMIR?

EMIR is the European Union's principal legislative response to the key commitments made by G20 leaders in respect of reform of the OTC derivatives markets at the Pittsburgh summit in September, 2009; it also contains some more general reforms of central clearing for all financial instruments. If you are based in a G20 country or a jurisdiction that is a member of the Financial Stability Board (the "FSB"), your local lawmakers may also be in the process of implementing similar reforms at a local level.

While EMIR deals with the clearing of certain OTC derivatives via a central counterparty (or "CCP"), risk mitigation techniques for non-cleared OTC derivatives and reporting requirements, reforms to existing investment services regulation ("MiFID II"), currently being negotiated between lawmakers, will deal with the on-venue trading of derivatives. This may also affect the way in which we trade derivatives with you. More information on how this may affect our trading relationship with you will be provided to you once these changes have been agreed.

2. Why is it relevant for counterparties outside of the EU?

EMIR places obligations on EU entities such as BNP Paribas with respect to their OTC derivatives trading activities with all of its counterparties, whether they are located inside or outside the EU. These requirements include a requirement for EU entities to classify all of their trading counterparties according to the categories designated by EMIR and to put in place certain documentation with all of their trading counterparties. For EU entities such as BNP Paribas it is impossible to comply with these requirements without the cooperation of our non-EU trading counterparties.

Although not compulsory for non-EU entities, the steps required to be taken under EMIR are intended to enhance the transparency and robustness of derivatives trading relationships and reduce legal disputes, so are of benefit to all counterparties regardless of where they are located. For EU entities they are also a regulatory requirement, and so it will be necessary to take these steps in order to ensure your trading relationship with your EU counterparts can continue without any risk of disruption.

Classification

3. What is my status (classification) under EMIR?

Provided that you are not established in the European Union or otherwise hold one of a finite list of financial services licenses from a European regulator (e.g. an EU banking or investment firm licence), then we will treat you as a third country entity ("TCE") for the purposes of EMIR. This means that, absent special circumstances, EMIR should not apply to you directly, but may still apply to OTC derivatives transactions that we enter into with you, we being an EU entity.

Our EMIR obligations in respect of transactions we enter into with you may vary depending upon both your own corporate status (e.g. commercial company, bank, fund manager, etc.) and the volume of outstanding derivatives business you have across all your uncleared OTC derivatives transactions with us and other counterparties. As a TCE, we will need to treat you as either:

- **A third country Financial Counterparty (or "FC")** – You will be a third country Financial Counterparty if (hypothetically) you would be licensed as an investment firm, a credit institution, an insurance or reinsurance firm, a fund manager or an occupational pension institution if you were established in the European Union. This occupational pension institution if you were established in the European Union. This will most likely be the case if you hold similar licence(s) in the jurisdiction(s) in which you operate, but could be the case in other circumstances as well (e.g. unlicensed third country hedge funds).
- **A third country non-financial counterparty (or "NFC"or "NFC-")** – This will be the most likely classification if you are a commercial entity undertaking limited derivatives business for hedging or investment purposes.
- **A third country NFC over the so-called "clearing threshold" (or "NFC+")** – NFCs who are over the so called threshold. This is most likely for those entities who undertake large volumes of derivatives business for investment rather than hedging purposes.

- **An exempt / partially exempt third country entity** – EMIR will not apply to transactions that we enter into with certain Central Banks and other entities charged with (or intervening in) the management of public debt. In addition, most provisions under EMIR (with the exception of the reporting obligation) will not apply where we deal with public sector entities that are owned and explicitly guaranteed by Central Government.

As a TCE, you are under no obligation to notify European regulatory authorities as to your status under EMIR (in contrast to e.g. EU established NFC+s). However, we need to know how to categorise you under EMIR to ensure that we only apply those obligations that are relevant to you. We can obtain this information from you, for example, via the recently published ISDA 2013 EMIR NFC Representation Protocol 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.

4. What are the benefits in confirming your status under EMIR?

There are potential benefits to you confirming your status to us, including the fact that, if you are an NFC and we have confirmation from you that you are below the clearing threshold, then our OTC derivatives transactions with you may benefit from an exemption from the pending regulatory capital charge for credit valuation adjustments ("CVA") under the Capital Requirements Regulation (part of the European implementation of Basel III). This could have a beneficial impact on the pricing of our trades with you. Absent such confirmation, ESMA has issued guidance that we would in principle need to treat our non-EU corporate counterparties as NFC+s, with the result that you may not benefit from this and other preferential treatment that you would otherwise enjoy as an NFC.

Please note that, in line with guidance issued by the European Securities and Markets Authority ("ESMA"), BNP Paribas 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 information which clearly demonstrates that information you have given in this regard is incorrect.

5. What are the clearing thresholds?

As its name suggests, the clearing threshold is a financial threshold that is principally relevant to whether or not we will be required to clear any "clearing eligible" OTC derivatives transactions that we enter into with any NFC, whether located in the EU or a third country. If you are an NFC and over the clearing threshold (and therefore an NFC+), you will be required to clear all clearing eligible hedging transactions that you enter into with us across each of the asset classes set out, irrespective of whether they are for hedging purposes, as and when the mandatory clearing obligation comes into effect, unless both you and the BNPP entity you face is out of scope of EMIR (though there may be other applicable local regulation which applies in that case).

In addition, whether you are above or below the clearing threshold is also relevant to certain other obligations under EMIR, including timely confirmation and portfolio reconciliation. Mandatory clearing is likely to be phased in later in 2014 – 2015 for the first phases of potentially clearing-eligible products such as interest rate swaps and CDS and will be preceded by a public consultation.

If you are a non-financial counterparty, it would be of great assistance to us if you could calculate whether or not you are over the clearing threshold or else whether it is likely that you will exceed the threshold in the near future.

The clearing thresholds are product-specific and are set at EUR1bn for credit derivatives and equity derivatives and EUR3bn for other asset classes, based on the aggregate gross notional value of your non-hedging derivatives. The details of calculating whether a firm is over the clearing threshold are complex, and we are happy to provide additional information on this aspect of EMIR if you are require this. You should note if any one NFC company in your group is over the clearing threshold, then all group companies which are NFCs are considered to be over the threshold.

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

This is correct. In determining whether or not an NFC's OTC derivatives positions exceed the relevant clearing threshold, it is necessary to include in the calculation all OTC derivatives contracts which that NFC and any other NFC in the same group have entered into which are not objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity".

In this context, the EMIR Regulatory Technical standards developed by ESMA to implement EMIR (the "RTS") set out in detail the criteria for establishing which OTC derivative contracts will be risk-reducing. For example, if the OTC derivatives contracts you enter into qualify for hedge accounting treatment under IFRS, those contracts will qualify for the hedging exemption.

7. How as a counterparty can you confirm your status under EMIR?

One of the easiest ways is going to be adhering to the ISDA published the ISDA 2013 EMIR NFC Representation Protocol (the "NFC Protocol"), which is designed to help market participants make representations in relation to their status. The benefit of this is that you only need to supply this information once and it gets communicated to all the other counterparties who are having to adhere to the protocols rather than having to deal with this bilaterally.

The other way of doing this, of course, because some entities may have sensitivities around making the information available on that basis, is to contact your counterparties, such as BNP Paribas, bilaterally and notify us that way, which is fine, as well. We're relatively open as to which methodology you wish to adopt to give us this information. You may find it's easier via the protocols.

Key Obligations

8. What are the key obligations that came into force on 15th September?

For third-country entities, one of the most important obligations came into force on 15th September is the requirements on us (as an EU credit institution subject to EMIR) to have in place, a written agreement with each of its counterparties in relation to:

- The terms on which the key trade terms of our OTC derivative contracts shall be reconciled (i.e. portfolio reconciliation); and
- The procedures and processes for disputes relating to the recognition or valuation of OTC derivative contracts or the exchange of collateral between us and our counterparties (i.e. dispute resolution).

These requirements are designed with our clients' best interests in mind, by seeking to encourage robust processes for the reconciliation of trades, minimise the risk of disputes in relation to the terms of agreed trades and ensure that, where disputes do arise, that they are resolved promptly.

These requirements form part of EMIR's risk mitigation techniques, which will also include bilateral margining requirements for non-cleared derivatives transactions with certain counterparties (in principle, NFC+s and other FCs), the framework for which has yet to be finalised. We will seek to update you further once the requirements are clear. Note that their requirements are not expected to come into force before 2015 and may be subject to a longer phase-in period in the case of some counterparties.

Timely Confirmation

9. How does EMIR impact on the confirmation of our transactions with you?

EMIR sets new deadlines for us to obtain timely confirmation of our OTC derivatives transactions with our counterparties and also requires such confirmation to take place by electronic means "where available" (e.g. where we deal with another counterparty that is a member of the same electronic confirmation platform, such as MarkitSERV or SwapsWire). The time we have to obtain timely confirmation from you will vary depending upon how you are classified for EMIR purposes and the nature of the transaction that we enter into with you.

Note that BNP Paribas 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 the relevant confirmation deadline.

10. Some counterparties may have some difficulties to confirm OTC contracts on time. What are the impacts if they are not able to?

BNP Paribas has to report late confirmations to the regulator.

Portfolio Reconciliation, Dispute Resolution and Portfolio Compression

11. In order to comply with the PR/DR obligations, what should we do?

To comply with this obligation, the key thing is to determine the frequency of reconciliations. There are two options – either adhere to the ISDA protocol which has been published during the summer or sign an equivalent bilateral agreement.

12. How does this protocol work?

The ISDA 2013 EMIR Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol is designed to meet the "written arrangements"/"agreed detailed procedures and processes" requirement in relation to Portfolio Reconciliation ("PR") and Dispute Resolution ("DR") respectively. From a contractual perspective, it takes effect by inserting the applicable language into each "protocol covered agreement", between each party which adheres to the protocol. The benefit of this is that when an entity adheres to the Protocol, the relevant changes are made as of the "implementation date" to each "protocol covered agreement" which that party has with each other entity who has also adhered. In this way, it avoids each party having to enter into multiple bilateral agreements with each of its counterparties to achieve this goal.

The coverage of the protocol is, as mentioned, each "protocol covered agreement" in place between the parties as of the time the second of the two parties adheres to the protocol (the "Implementation Date"). This includes (i) an ISDA in place between the parties; (ii) any other master agreement in relation to derivatives between the parties; (iii) any ISDA Long Form Confirmations in place between the parties (which also includes ISDA LFCs entered into between the parties after the Implementation Date); and (iv) any other agreement in relation to derivatives (including a non-ISDA LFC). I would also mention in passing that there are special rules in relation to agreements entered into by agents.

Certain agreements are excluded from the scope of this protocol. This includes agreements which (i) exclude the application of the protocol; (ii) agreements which already cover the matters addressed in the protocol; as well as (iii) any agreement which is guaranteed, and the effect of the protocol as between the two counterparties parties would be to discharge the guarantee. In this case, however, if the guarantor also adheres, then the relevant consent is deemed provided.

ISDA has provided helpful FAQs in relation to the protocol and how to adhere to it, which can be found on the following URL: http://www2.isda.org/functional-areas/protocol-management/faq/15

13. If we have not signed up to ISDA Protocol or otherwise put in place a bilateral agreement relating to PR/DR with BNP Paribas by 15th September, what is the impact?

The strict reading of the regulatory requirements under EMIR in this regard is that the relevant agreements and procedures must be in place to enable trading to continue post 15th September. That being said, a very important consideration here is the view taken by the regulator of the party in question. As a general matter, there seem to be some informal views being expressed by certain European regulators that the focus must be on getting the necessary agreements in place as soon as possible even if trading is to continue after this date without the agreement in question being in place. From our perspective, whilst as a general matter BNP Paribas will be prepared to maintain our trading relationships with counterparties for a certain period after 15th September, we would wish to have the agreement in place (which may be best achieved via adherence to the PR/DR Protocol) as soon as possible to enable the formal requirements to be met, or to understand what is still needed from our counterparty's perspective, for such an agreement to be put in place.

14. If both parties have already adhered to the ISDA portfolio reconciliation and dispute resolution protocol, is there anything else to do in order to comply with portfolio reconciliation and dispute resolution obligations?

By adhering to the protocol, both parties have agreed on the arrangements under which they will undertake portfolio reconciliation. BNP Paribas will then be able to trigger the first reconciliation before the end of the agreed reconciliation period. No further action is required from our clients in that case, other than where they have indicated that they are data senders (in which case they will need to be ready to send the relevant data as agreed).

15. What happens if BNP Paribas is already reconciling their portfolio with you?

BNN Paribas operational team will first check if the parameters of the reconciliation currently processed match EMIR requirements as described in the contractual agreement that is in place between us. If the frequency used is different from the one required under EMIR, we would either change it if the current frequency is lower than EMIR frequency, keep it if the current frequency is higher than EMIR frequency, or set-up a separate reconciliation if the client requires it.

16. Regarding the 2-way reconciliation in Tri-Optima, is there a Privacy Agreement between BNP Paribas and the Third-Party service provider?

Tri-Optima do all our Bilateral reconciliation. BNP Paribas' agreement with Tri Optima includes privacy terms. BNP Paribas will need consent from clients to upload their portfolios into TriOptima.

Trade Reporting

17. I understand that EMIR also contains trade reporting requirements. Will these apply to our transactions with you, even if we are a TCE?

Yes. Whilst you yourself will not become subject to any direct reporting requirements under EMIR, as an EU Financial Counterparty we will be obliged to report details of all our derivatives transactions (including exchange-traded derivatives and those OTC derivatives that qualify for the hedging exemption) to licensed trade repositories ("TRs"), including information on our counterparties on those trades. This reporting will extend to the back-reporting of derivatives transactions that we entered into before EMIR came into force on 16th August 2012 and that were outstanding on that date, as well as those transactions that we have entered into since. At this time, the first trade reporting obligations have been postponed to February 2014, with reporting of most (if not all) OTC and exchange-traded derivatives due to commence on that date (though we don't have the final list at present, since this depends upon the scope of the registration of the authorised TRs).

We recognise that you may also be subject to derivatives reporting requirements in the jurisdiction(s) in which you operate. Where your reporting requirements overlap with the reporting requirements under EMIR it is possible that we may be able to assist by reporting such transactions on your behalf, e.g. where your reporting obligation can be satisfied by reporting details of your trade to a global trade repository such as DTCC. BNP Paribas is in the process of developing potential client reporting services and should be in a position to circulate further information on these services in due course. If the requirements do not match or reporting to a global repository is not sufficient for your purposes, reporting to a local TR as well as to an EU registered TR may be required. We will endeavour to keep you updated on whether cross border cooperation between international regulators will enable European authorities to accept equivalent standards on reporting in your jurisdiction, thus avoiding potentially duplicative reporting.

Note that EMIR places strict obligations of confidentiality on TRs with a view to ensuring the confidentiality of the data that they receive and that it is not used for ancillary purposes; similar obligations apply to ESMA and other competent authorities discharging obligations under the regulation. We will likely require you to consent to our reporting the details of the trades we do with you to ensure we do not breach any contractual or other legal obligations of confidentiality we owe to you. ISDA have published a Reporting Protocol, which is not specific to EMIR.

Conclusion

18. What are the upcoming deadlines?

- Trade reporting requirements that will come into force for European Counterparties on 12th February 2014
- Clearing Obligations that will enter into force later in 2014
- The exchange of initial margining as far out as 2015

19. How can we help?

ISDA has published two protocols to assist parties in meeting the EMIR obligations:

- **On 8 March 2013**, ISDA published the ISDA 2013 EMIR NFC Representation Protocol (the "NFC Protocol"). The NFC Protocol is designed to help market participants make representations in relation to each party's NFC status.
- **On 19 July 2013**, ISDA published the ISDA 2013 EMIR Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol (the "PR/DR Protocol"). It is designed to address the September 15th obligations in relation to portfolio reconciliation and dispute resolution described in Question 6 above. It also includes some helpful confidentiality waivers for reporting purposes, looking ahead to the phasing in of TR reporting in 2014.

BNP Paribas has adhered to both protocols. Both protocols are open to parties established outside the European Union and we would encourage all clients with whom we have ISDA Master Agreements to adhere to the Protocols as the most efficient way of assisting us in meeting our various EMIR obligations. Whilst the NFC Protocol is specific to counterparties using ISDA Master Agreements, the PR/DR Protocol is open to parties using other documentation as well. The protocols are open to both ISDA members (such as BNP Paribas) and non-ISDA members. The protocols are both "evergreen" protocols, which means that they remain open for adherence until ISDA designates a closing date.

BNP Paribas will seek to obtain certain representations from you confirming your status under EMIR and for the most part we will attempt to do so via this NFC Protocol. Some clients may not choose to adhere to the NFC Protocol and instead choose to notify BNP Paribas bilaterally. As set out previously, 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. In the case of the PR/DR Protocol, adhering to the Protocol allows us to satisfy our September 15th obligations without needing to execute bilateral agreements or other documentation.

20. In summary, what we require from you?

- Confirm your classification under EMIR
- Adhere to the PR/DR protocol or execute an equivalent agreement and confidentiality waiver.

Thank you all for attending the EMIR Regulation Call. Distribution of this Q&A will follow shortly together with a request for feedback.