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To EFET- Market Supervision Committee

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Commodity derivative clearing under EMIR

A cross jurisdictional analysis

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A. Introduction

Subject of this analysis is to compare the international treatment of commodity derivative transactions relating to the clearing obligation and related requirements with a particular focus on non-financial market participants and their regulatory obligations. Overall aim is to identify

- the regulatory objectives of OTC-derivatives regulation,
- the different legal approaches to achieve them,

and to determine

- the regulatory burden associated with these approaches.

In a **first step**, we are outlining the obligations under **EMIR**[1] and its corresponding delegated regulations ("**CDR 149/2013**")[2] in relation to the clearing obligation of market participants including the positions taken by the European Securities and Markets Authority[3] ("**ESMA**"). We further put this in relation to other national OTC regimes which explicitly take up the EMIR approach such as the **Swiss regime** under FinfraG[4] in order to identify the regulatory headroom within the broader EMIR-concept.

In a **second step**, we compare the main elements of EMIR with other international approaches serving a similar purpose.

With regard to the size of the underlying market and the number and variety of international market participants, we considered the **USA**, **Australia** and **Singapore** as relevant

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[1] 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 ("**EMIR**"); available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32012R0648&from=EN; amended by Regulation (EU) 2019/834 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 648/2012 as regards the clearing obligation, the suspension of the clearing obligation, the reporting requirements, the risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty, the registration and supervision of trade repositories and the requirements for trade repositories ("**EMIR Refit**"); available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32019R0834.

[2] Commission Delegated Regulation (EU) No 149/2013; EUR-Lex - 02013R0149-20180103 - EN - EUR-Lex (europa.eu) as amended by Commission Delegated Regulation (EU) No.2017/2175).

[3] In particular in its Q&A's, ESMA, Questions and Answers Implementation of the Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories (EMIR) ("**ESMA Q&As**"); available at https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf.

[4] SR 958.1 - Bundesgesetz vom 19. Juni 2015 über die Finanzmarktinfrastrukturen und das Marktverhalten im Effekten- und Derivatehandel (Finanzmarktinfrastrukturgesetz, FinfraG) (admin.ch).

competing jurisdictions. In that regard, we have limited our assessment to jurisdictions which are members of the Financial Stability Board[5] and have largely complied with the G20 commitments of the Pittsburgh summit as indicated in the FSB progress report[6].

We identified as relevant distinction criteria and paid particular attention to

- which clearing thresholds exist;
- which entities are in scope;
- which products and activities are in scope;
- the extraterritorial reach of the regulation;
- which transactions contribute to the thresholds;
- what exemptions from the threshold calculation exist (e.g. hedging exemptions) and how they are defined;
- the calculation methodology including intra-group treatment, set-off and netting effects.

In order to assess and highlight the implications we focussed on practical examples relating to energy commodity derivatives used in relation to renewable energy infrastructure but do not limit our conclusions to this sector of commodity derivatives.

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[5] The Financial Stability Board (FSB) coordinates at the international level the work of national financial authorities and international standard-setting bodies in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies. Its mandate is set out in the FSB Charter, which governs the policymaking and related activities of the FSB.

[6] FSB, OTC Derivatives Market Reforms, Note on implementation progress for 2020, 25.November 2020, out of all jurisdictions, **Switzerland** and **Australia** are the two jurisdictions with the **highest degree of target achievement**. See OTC Derivatives Market Reforms: Note on implementation progress for 2020 (fsb.org).

B. High level results

As a result of this comparison, we could conclude that the approach used by the EU under EMIR is the most restrictive of all approaches, poses significant burden on non-financial commodity traders and is thereby expected to hamper market liquidity and the availability of bilateral hedging. It fosters regulatory market steering and development instead of promoting the best commercial solution, without producing more financial stability or social welfare.

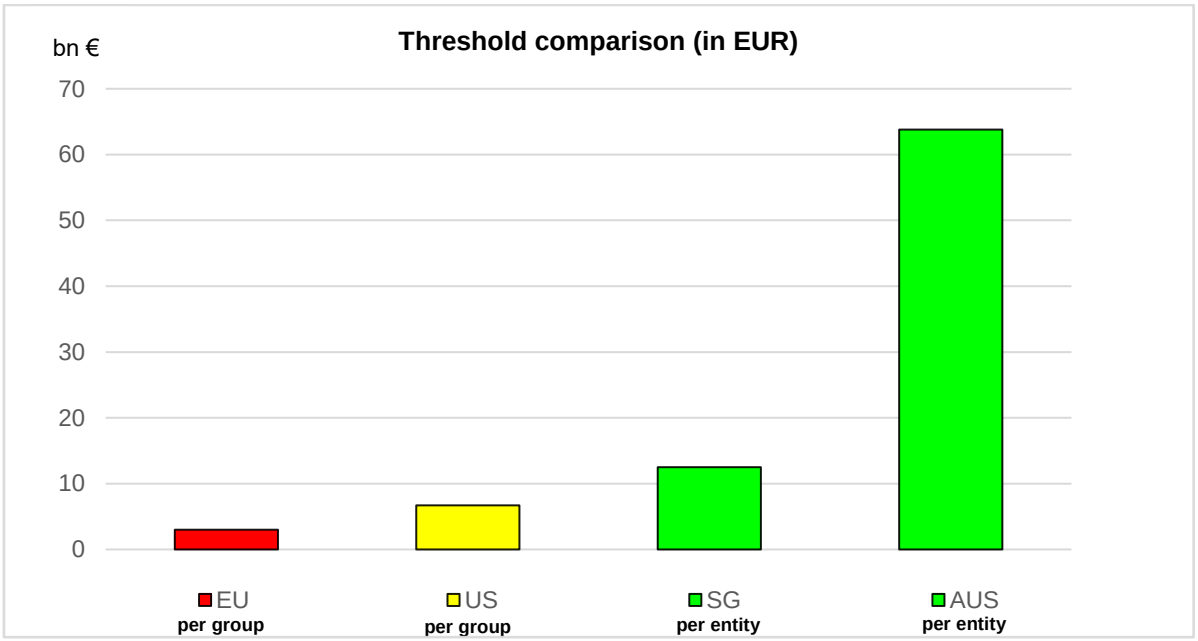
In the context of using energy commodity derivatives to mitigate risks of investments needed for the **energy transition**, this may have detrimental effects on the market and lead to increasing costs of transactions. This is of particular importance for investments into energy infrastructure such as wind parks, solar installations and hydrogen infrastructure which carry long term market risk and may require corresponding long term hedging with derivatives. Such hedging, however, requires the presence of market counterparties which are willing and able to take such risk into their own books and provide hedging options to the market.

Our conclusions are highlighted by the following **key findings**:

- only the EU applies its regime to all trading activities around the globe without restriction,
- only the EU includes cleared and physically settled exchange traded derivatives into the threshold calculation,
- a number of jurisdictions limit the application of OTC-clearing regulation entirely to financial institutions,
- those which include non-financial market participants, in particular the US and the EU, offer privileges for hedging transactions which are not considered for the clearing threshold. However, the definition of eligible risks for hedging under EMIR is rather restrictive and the privilege correspondingly narrow.

At the same time, the EU offers a commodity derivative clearing threshold of **3 bn EUR** per group against **8 bn USD** per group in the US, **20 bn SGD** per entity in Singapore and **100 bn AUD** per entity in Australia.

Table 1



To summarize our conclusions:

- **The EU offers the lowest threshold applicable to the largest set of entities, products and activities.**

The results of our analysis are further visualized in the following table:

Table 2 – Commodity trading and the clearing obligation (global)

	EU (EMIR)	US (DFA)	AUS ASIC (Derivative Transaction Rules)	SG (Clearing of Derivatives Contracts Regulations)
I. Purpose and scope	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)
1. Threshold Amount	3 bn EUR - per group -	8 bn USD - per group -	100 bn AUD - per entity -	20 bn SGD - per entity -
2. In-scope entities	All entities, including non-financial entities and end-users	"Dealers": Swap Dealers and Major Swap Participants; no commercial end users	Only financial entities (clearing entities)	Only banks
3. In-scope activities	Any trading activity	"dealing activities"	Trading in representing capacity and personal capacity	Any trading activity
a) third party dealing	Yes	Yes	Yes	Yes
b) own account dealing	Yes	Only if separate P&L center or resources specifically allocated to such business	Yes	Yes

	EU (EMIR)	US (DFA)	AUS ASIC (Derivative Transaction Rules)	SG (Clearing of Derivatives Contracts Regulations)
4. In-scope products	"OTC-Derivatives"	"Swaps"	"OTC-Derivatives" for financial settlement, excluding venue traded instruments	"OTC-Derivatives", excluding venue traded instruments
a) includes physically settled products	Yes	No, with limited practically irrelevant exemptions	No	Yes
b) includes physically settled ETD on third country venues	Yes if venue not individually recognized as equivalent	No, excluded due to physical settlement and in most cases not considered Swaps	No, excluded due to physical settlement and not considered OTC	No, not considered OTC
c) includes financially settled ETD on third country venues	Yes, if venue not individually recognized as equivalent	Practically not, products usually not considered Swaps, inclusion would further depend on US-impact, indicated by involvement of a US person, guaranteed entity or significant risk subsidiary; general exclusion of certain foreign boards of trade	No, not considered OTC due to general recognition of major third country venues in the law	No, not considered OTC
5. Geographical coverage	Global reach for all in-scope instruments and activities	All activities of US persons. Activities of affiliated non US-persons only if	Only Australian incorporated entities, entities representing Australian schemes or	Only Singaporean entities and instruments "booked in Singapore"

	EU (EMIR)	US (DFA)	AUS ASIC (Derivative Transaction Rules)	SG (Clearing of Derivatives Contracts Regulations)
		guaranteed entities or significant risk subsidiaries or with US persons or guaranteed entities	transactions booked in Australian branches or entered into in Australia	
a) third country business of affiliates in scope	Yes	No, if not itself a guaranteed entity or significant risk subsidiary or with US persons or guaranteed entity counterparties	No	No
6. Includes intra-group transactions	Yes	No	No	Yes
7. Privileged transactions not counting against threshold	Yes	Yes	No, concept not applied	No, concept not applied
a) Hedging	Yes, if objectively measurable as reducing risks relating to entity's commercial activity	Yes, if hedging physical positions or "relevant facts and circumstances" test fulfilled	No, concept not applied	No, concept not applied
i) third party commercial positions eligible for hedging	No	Generally not but case-by-case analysis required	No, concept not applied	No, concept not applied

	EU (EMIR)	US (DFA)	AUS ASIC (Derivative Transaction Rules)	SG (Clearing of Derivatives Contracts Regulations)
ii) financial positions eligible for hedging	In general yes, depending on underlying risk	In general yes, depending on underlying risk	No, concept not applied	No, concept not applied
b) netting effects recognized	Yes, limited	No	No	No
II. Threshold 1. amount and reference	3 bn EUR Commodity threshold - per group -	8 bn USD Single threshold - per group -	100 bn AUD Single threshold - per entity -	20 bn SGD Single threshold - per entity -
2. Reference period for calculation	Every 12 months as aggregate month-end average position for the previous 12 months	12 months rolling average of deals concluded	Position crossing at two consecutive calculation dates (one calculation date per quarter)	Position at last day of each of the last 4 quarters

[Table 2 – Commodity trading and the clearing obligation (global) contd.]

C. Jurisdictional comparison

I. EU – EMIR

1. In-scope entities

EMIR follows a comprehensive approach as regards the in-scope entities to which the clearing obligation applies. Article 4 (1) of EMIR[7] stipulates a clearing obligation for EU firms that are counterparties to OTC derivative contracts[8]. In this regard, EMIR distinguishes between financial counterparties[9] ("**FC**") and non-financial counterparties[10] ("**NFC**") but does include both into the full set of obligations, if the quantitative prerequisites are met.

FCs are subject to the clearing obligation under EMIR for **all** classes of OTC derivatives if they exceed the clearing threshold or if they do not calculate their position at all[11]. NFCs are only subject to the clearing obligation under EMIR for all classes of OTC derivatives if they do **not** calculate their positions. If they do calculate their positions and exceed the clearing threshold, they are only subject to the clearing obligation for the class of derivatives in which the clearing threshold was exceeded[12].

For all entities, the distinction is made by determining their actual positions against the clearing threshold.

2. In-scope products

a) General approach

In particular from a product perspective, EMIR has a very broad scope and covers the majority of traded OTC derivative contracts irrespective of settlement.

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[7] When referring to the "EMIR", the consolidated version after EMIR Refit is referred to if not specified otherwise.
[8] See Article 2 (5) and (7) of EMIR.
[9] As defined in Article 2 (8) of EMIR, meaning inter alia banks, insurers, asset managers.
[10] As defined in Article 2 (9) of EMIR, meaning all undertakings established in the EU other than Central Counterparties ("**CCP**") as defined in Article 2 (1) of EMIR and FCs.
[11] See Article 4a (1)(c) of EMIR.
[12] See Article 10 (1)(c) of EMIR.

According to Article 2 (5) of EMIR, the terms 'derivative' or 'derivative contract' mean all financial instruments as set out in number (4) to (10) of Section C of Annex I to Directive 2004/39/EC[13], therefore including inter alia:

- options, futures, swaps, forward rate agreements and any other derivative contracts relating to securities, currencies, interest rates or yields, emission allowances or other derivatives instruments relating to commodities which may be settled physically or in cash;[14]
- any other derivative contract relating to commodities not being for commercial purposes, which have the characteristics of other derivative financial instruments;[15]

as well as

- derivative contracts relating to i.a. assets, rights, obligations indices and measures which have the characteristics of other derivative financial instrument, which may be settled physically or in cash[16].

"OTC"[17] derivative contracts are derivative contracts the execution of which does not take place on a **Regulated Market** within the meaning of Article 4(1) no.14) of MiFID II or on a third-country market considered to be equivalent to a Regulated Market in accordance with Article 2a[18] of EMIR. It is important to note that the qualification of a derivative contract as "OTC" does therefore not depend on characteristics of the respective contract or of the counterparties but the place of execution[19].

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[13] Replaced by Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU ("**MiFID II**"); available at https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065&from=DE.
[14] Annex I C(4)-C(6) MiFID II.
[15] Annex I C(7) MiFID II which includes third country venue trade instruments, see Art. 7 CDR 565/2017.
[16] Annex I C(10) MiFID II.
[17] See Article 2 (7) of EMIR.
[18] Article 2a of EMIR reads: "*For the purposes of Article 2(7) of this Regulation, a third-country market shall be considered to be equivalent to a regulated market within the meaning of Article 4(1)(14) of Directive 2004/39/EC where it complies with legally binding requirements which are equivalent to the requirements laid down in Title III of that Directive and it is subject to effective supervision and enforcement in that third country on an ongoing basis, as determined by the Commission in accordance with the procedure referred to in paragraph 2 of this Article*".
[19] See ESMA Q&As, p. 16.

In addition, EMIR provides for a negative distinction in the definition. Any derivative contract counts as OTC derivative contracts as long as it is **not** executed on an Regulated Market in the EU or a market recognized as equivalent[20] to such Regulated Market. In the understanding of the EU under Art. 2a EMIR, such recognition requires a formal act and absent such act, qualitative criteria with regard to the venue in question, do not matter. As a consequence, venue traded instruments may be in scope regardless of such venue in fact meeting the criteria of a supervised exchange and irrespective of actual clearing of such venue traded products similar to exchange traded derivatives at Regulated Markets.

b) Inclusion of physically settled products

By referring to the derivative contracts listed in Annex I C of MiFID II, EMIR inter alia includes OTC derivative contracts which may be settled physically. These are C(6), C(7) and C(10) products with the exemption of wholesale energy products that must be physically settled under C(6) and are back-exempt under the so called REMIT-carve out if they were traded on an Organized Trading Facility[21].

c) Inclusion of transactions at third-country regulated markets

Since every OTC derivative contract would have to be included in the clearing threshold calculation by the respective undertaking and due to the negative distinction explained above, any derivative contract executed on a third country market, which has not been recognized as equivalent, has to be regarded as an OTC derivative contract relevant for the threshold. ESMA has published a list of regulated markets, which have been recognized as equivalent[22]. This list currently does not include, for example, any of the important and highly frequented regulated markets of China, the UAE, such just evolving in Turkey or the Ukraine or also such based in the UK like LME and ICE Futures Europe.

Therefore, with regard to the UK, ESMA has taken the view that new derivative contracts, the execution of which takes place in a UK market **after** such market has become a third

[20] See ESMA Q&As, question 1, p. 15 et seqq.
[21] As defined in Art. 4 (1) no.23 but by definition only including EU-entities and not privileging similar third country venues.
[22] ESMA, List of third-country markets considered as equivalent to a regulated market in the Union for the purposes of the definition of OTC derivatives, January 26, 2017; https://www.esma.europa.eu/sites/default/files/library/equivalent_tc-markets_under_emir.pdf.

country market not considered to be equivalent to a Regulated Market (according to Article 2a of EMIR), are considered OTC derivative contracts under Article 2 (7) of EMIR[23].

3. In-scope activities

EMIR directly applies to OTC derivative contracts that are not executed on Regulated Markets concluded for whatever purpose and does not stipulate any qualitative criteria with regard to the performed activities or services associated with those contracts. Consequently, all possible trading activities of the in-scope entities are covered according to Annex I A MiFID II regardless of its qualification. EMIR does in particular not distinguish between sole own account trading on one hand and dealing on own account as service for third parties on the other.

Therefore, EMIR not only covers most of the traded products and every trading entity but also any form of trading business, regardless of its purpose. The basic coverage is therefore **particularly wide**.

4. Threshold calculation methodology

The clearing obligation does not apply if the clearing thresholds specified in CDR 149/2013 are not exceeded. Entities above the threshold are commonly referred to as FC+ or NFC+, entities below the threshold as FC- or NFC- correspondingly.

a) Threshold amount

According to Article 11 of the CDR 149/2013, the clearing thresholds values for the purpose of the clearing obligation are:

(a) EUR 1 billion in gross notional value for OTC credit derivative contracts;

(b) EUR 1 billion in gross notional value for OTC equity derivative contracts;

(c) EUR 3 billion in gross notional value for OTC interest rate derivative contracts;

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[23] See ESMA Q&As, p. 17, updated answer to question 1, December 21, 2020.

(d) EUR 3 billion in gross notional value for OTC foreign exchange derivative contracts;

(e) **EUR 3 billion in gross notional value for OTC commodity derivative contracts and other OTC derivative contracts not provided for under points (a) to (d).**

b) Reference period

The thresholds listed above have to be calculated every 12 months as aggregate month-end average position for the previous 12 months[24]. OTC derivative contracts entered into for a period of more than a year may therefore be counted more than once or even several times until their expiry.

c) Geographical coverage – third country business of affiliates

From a product perspective, EMIR applies without limitation to all OTC derivative contracts of counterparties regardless of the country of their execution. EMIR and MiFID II definitions do in general apply without any geographical or jurisdictional restriction. Such necessary link to EU-markets is only introduced on the level of the in-scope entities which are bound by the actual EMIR obligations[25]. As stipulated by Art. 2 no. 9 EMIR, these are all and any EU-incorporated entities, either as FC or as NFC. Even if only those EU-incorporated entities are subject to EMIR-obligations, in order to establish the scope of their obligations, the entire group business is considered, including non EU-activities. In particular the calculation of the positions in OTC derivative contracts of such entity has to be performed on a **group-wide basis**. The term “group” includes all subsidiaries, sister and parent companies wherever the ultimate parent company is established[26]. According to Art. 10 (3) EMIR, this definition extends to all OTC-Derivatives entered into by *non-financial group entities*, a term which, opposed to *non-financial counterparty*, is **not** restricted to EU-entities. Consequently, every EU-incorporated entity has to include in its own threshold calculation each and every OTC-

[24] See Articles 4a (1) and 10 (1) of EMIR and ESMA Q&As, p. 20.
[25] i.e. clearing, reporting and risk mitigation.
[26] See ESMA Q&As, OTC answer 3 (d), p. 21.

derivative - wherever concluded - of any of its non-financial group entities wherever established[27].

As a result of this "global group approach", an **EU-entity might cross the threshold solely caused by trading activities of its non-EU affiliates** executed with other non-EU-counterparties, either OTC or at non-EU trading venues not considered equivalent**.**

It could pass the threshold even if the EU-Counterparty had not concluded **any single transaction itself** nor would there be any single EU-transaction present in its group. It would even not matter if in such event **the EU-entity would not assume any corporate or contractual liability for the transactions of its non EU-affiliates.**

Consequently, the EU-clearing threshold could be passed **absent of any risk exposure to EU-markets** whatsoever.

d) Inclusion of intra-group transactions

Any entity calculating its position in OTC derivative contracts under EMIR, shall generally include all OTC derivative contracts entered into by that entity or by other entities within the group to which that entity belongs[28].

According to ESMA, if two entities belonging to the same group enter into an intra-group transaction[29] with each other, **both sides of the transaction** are to be counted. The total contribution to the group-level threshold calculation would therefore be at least[30] twice the

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[27] Apparently, with regard to the reporting obligation, EMIR follows a different approach towards third country parent undertakings where it declares the exemption contained in Art. 9 (1) inapplicable for intra-group transactions where the parent is a third country entity, see Q&A's, answer to question TR 51 (m), p. 120.

[28] See Articles 4a (3) and 10 (3) of EMIR.

[29] Already narrowly defined by Article 3 (1) of EMIR: *In relation to a non-financial counterparty, an intragroup transaction is an OTC derivative contract entered into with another counterparty which is part of the same group provided that both counterparties are included in the same consolidation on a full basis and they are subject to an appropriate centralised risk evaluation, measurement and control procedures and that counterparty is established in the Union or, if it is established in a third country, the Commission has adopted an implementing act under Article 13(2) in respect of that third country.* Group Transactions not meeting this definition are ordinary third party transactions.

[30] Transactions may even count three times if first executed at the market and secondly sleeved through from the market facing entity to its subsidiary.

notional value of the contract[31]. Such double counting may further inflate the usage of the clearing threshold without adding to the overall systemic risk of the activity.

e) Privileged transactions not counting against the threshold

(i) Hedging

Unlike FCs, NFCs can exclude from the calculation certain OTC derivative contracts that are objectively measurable as reducing risks relating to their commercial activity ("**hedging**")[32].

The prerequisites for a transaction to be considered "*objectively measurable as reducing risks relating to their commercial activity*" are defined in further detail in Article 10 of CDR 149/2013. It is important to note that whether an OTC derivative contract is covered by the definition is evaluated based on its objective suitability to reduce risks directly relating to the commercial activity or treasury financing activity **of the non-financial counterparty or of its group**. In addition, there does not have to be a direct link between the hedging contract and the risk to be mitigated, rather the definition also includes proxy hedging and macro or portfolio hedging[33].

To fulfil the definition in Article 10 CDR 149/2013, the contract, by itself or in combination with other derivative contracts, directly or through closely correlated instruments, has to meet one of the following criteria:

> *(a) it covers the risks arising from the potential change in the value of assets, services, inputs, products, commodities or liabilities that the non-financial counterparty or its group owns, produces, manufactures, processes, provides, purchases, merchandises, leases, sells or incurs or reasonably anticipates owning, producing, manufacturing, processing, providing, purchasing, merchandising, leasing, selling or incurring in the normal course of its business*;

[31] Absent any other privilege kicking in, See ESMA Q&As, OTC answer 3 (d) p. 21.
[32] See Article 10 (3) of EMIR.
[33] ESMA Q&As, OTC answer 10 (c) p. 29.

(b) it covers the risks arising from the potential indirect impact on the value of assets, services, inputs, products, commodities or liabilities referred to in point (a), resulting from fluctuation of interest rates, inflation rates, foreign exchange rates or credit risk;

*(c) it qualifies as a hedging contract pursuant to International Financial Reporting Standards ("**IFRS**") adopted in accordance with Article 3 of Regulation (EC) No 1606/2002 of the European Parliament and of the Council.*

In cases of portfolio or macro hedging by an NFC, there may not be a one-to-one link between a specific transaction in OTC derivative and a specific risk directly related to the commercial activity or treasury financing activities entered into to hedge it. The implementation of the complex risk management systems potentially used for that kind of portfolio hedging would generally be assessed by the relevant national competent authority on a case by case basis[34].

In cases where an intra-group transaction and a corresponding transaction between a group entity and an external counterparty occur, both transactions might be considered as hedging contracts. This, according to ESMA, is because in a non-financial group, typically there is one entity that is specialised in dealing in derivatives with entities outside the group (the trading or market facing entity). This external derivative contract mirrors one or more derivative contracts with entities within the group if the internal contract can be considered a hedging contract. On the contrary, where the derivative contracts concluded by an NFC in the group that is not the trading entity do not qualify as hedging contracts, then the corresponding external contracts should not be considered as hedging contracts either[35].

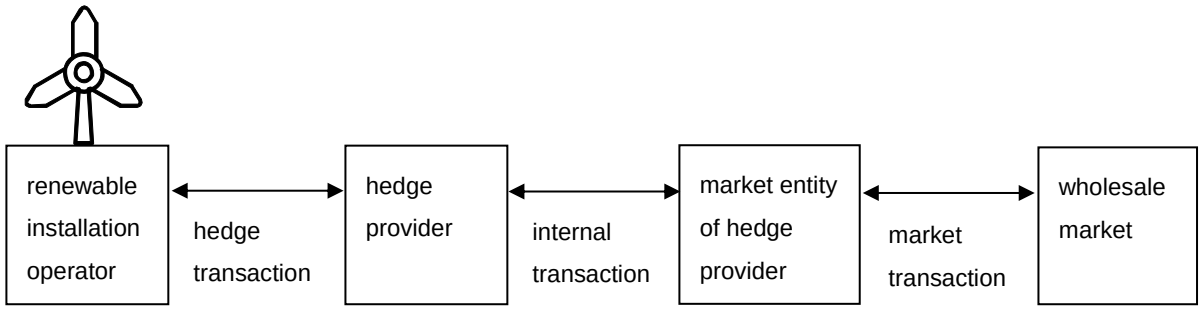
By way of example, this may have the effect that **offering** a long term **hedge** in favour of a renewable energy operator may count against the clearing threshold **multiple times** as none of these would be considered hedging for the hedge provider:

- the initial transaction of the hedge provider with the operator of the renewable installation;

[34] See ESMA Q&As, OTC answer 10 (c) p. 29 et seq.; here, ESMA also lists the criteria to be fulfilled by the risk management systems.
[35] See ESMA Q&As, OTC answer 3 (e) p. 21 et seq.

- a second internal group transaction with the market facing entity of the hedge provider;
- the external transaction at the market of the market facing entity of the hedge provider.

To visualize this structure:



[sample deal flow renewable hedge between operator as client and third party hedge provider]

(ii) Netting

According to ESMA, netting of one's positions per counterparty and contracts is permissible. After such netting, the absolute notional value of all net positions (calculated based on the notional amounts of the contracts) should be added up. Netting per contracts and counterparty should be understood as fully or partially offsetting contracts having **exactly** the same characteristics (type, underlying, maturity, etc.) with the only exception being the direction of the trade and notional amount (in case of partial offset) concluded with the same counterparty[36]. This concept of netting applied by ESMA falls short of the calculation of netted exposures towards counterparties which is applied in the market. Here, in line with the applicable legal opinions[37], all nettable positions in any commodity with the same

[36] See ESMA Q&As, OTC answer 3 (f) p. 22.
[37] As obtained from time to time by EFET, ISDA or other industry associations.

counterparty would be netted out, not limited to those having the exactly same characteristics.

f) Calculation includes voluntarily cleared derivative contracts

As according to Article 4a(3) and Article 10(3) of EMIR, OTC derivatives are to be included regardless of whether they are cleared or not, OTC contracts that are being cleared on a voluntary basis shall also be included in the calculation of the clearing thresholds[38].

Margining, collateralization or other forms of risk mitigation techniques also do not exclude a contract from counting against the threshold.

In summary, EMIR defines the subset of in-scope products, activities and products **particularly broad**. It has to be noted that not only all group activities anywhere on the globe are in scope but also such transactions at not formally recognized third country venues which would in fact not be viewed as OTC but exchange traded if such venue was based within the EU and consequently left out of scope for threshold calculation.

With regard to the extraterritoriality approach in calculating the threshold, **a particular impact test** regarding the impact on the stability of **EU-markets**, **is not foreseen.**

[38] See ESMA Q&As, OTC answer 1 (d) p. 16 and OTC answer 3 (d) p. 21.

5. EMIR-related third country regimes: Switzerland

Prior to comparing the EU-approach on a global scale, we aim to identify regulatory options within the EMIR-approach by comparing it with regimes which explicitly base their own system on the EMIR-model, such as Switzerland.

a) General

The regulation of OTC-derivatives including the clearing mandate in Switzerland is to a large extent comparable to the EMIR-regime in the EU. Reason is, that with the adoption of the FinfraG[39] and the respective ordinance in the FinfraV[40], Switzerland aimed to establish a similar and equivalent regime compared to EMIR and EU-financial regulation in general[41]. For this reason, we did **not** include Switzerland into the global clearing comparison as we view both as largely the same concept. However, albeit this approach being pursued, there are still noteworthy differences in the application and reach of the respective provisions which indicates that there is legislative headroom to amend EMIR without jeopardizing its functioning.

The threshold is set by delegated ordinance for commodity derivatives at a level of **3.3 bn CHF**[42] and which applies to OTC-trading activities of non-financial entities only. Financial counterparties are subject to an integrated single threshold of 8 bn CHF. Entities below the respective thresholds are considered small non-financial and small financial entities.

b) In-scope entities

FinfraG applies to both financial and non-financial entities as per the definition in Art. 93 (2) and 93 (3) FinfraG. Non-financial entities are all residual entities which do not fall under any

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[39] SR 958.1 - Bundesgesetz vom 19. Juni 2015 über die Finanzmarktinfrastrukturen und das Marktverhalten im Effekten- und Derivatehandel (Finanzmarktinfrastrukturgesetz, FinfraG) (admin.ch).
[40] SR 958.11 - Verordnung vom 25. November 2015 über die Finanzmarktinfrastrukturen und das Marktverhalten im Effekten- und Derivatehandel (Finanzmarktinfrastrukturverordnung, FinfraV) (admin.ch).
[41] BBl 2014 7483 - Botschaft zum Finanzmarktinfrastrukturgesetz (FinfraG) (admin.ch).
[42] Art. 88 para. 1 FinfraV based on Art. 100 FinfraG as part of a separated threshold approach per asset class.

of the listed categories for financial entities and would consequently comprise the non-licensed sector of utilities, energy traders and commercial end users of OTC-derivatives.

c) In-scope products

i) OTC-derivatives

In scope of the clearing mandate under FinfraG are OTC-derivatives which comprise derivatives as defined per Art. 2c[43] and which are not executed at a trading venue[44]. Trading venue under FinfraG means any of either a stock exchange or a multilateral trading facility.

Both types of trading venue are defined on a qualitative level in FinfraG without the need for a formal recognition by any Swiss Authority[45] for the qualification of the products traded thereon.

- *Stock exchange* means an institution for multilateral securities trading where securities are listed, whose purpose is the simultaneous exchange of bids between several participants and the conclusion of contracts based on non-discretionary rules;

- *multilateral trading facility* means an institution for multilateral securities trading whose purpose is the simultaneous exchange of bids between several participants and the conclusion of contracts based on non-discretionary rules without listing securities[46].

As a consequence, bilaterally traded derivatives are in scope, venue traded **including third country venue traded instruments** are **out of scope** of the regulation. This lack of the requirement of formal recognition of third country

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[43] *Derivatives or derivatives transactions: financial contracts whose value depends on one or several underlying assets and which are not cash* (Kassa=spot) *transactions.*
[44] Art. 97 (1) FinfraG.
[45] The indeed existing recognition requirement under Art. 41 FinfraG refers to the granting of direct market access to Swiss participants to such facilities, not to the recognition of the respective products as either ETD or OTC-derivatives, see "*Wegleitung für Gesuche betreffend die Anerkennung als ausländischer Handelsplatz nach Art. 41 FinfraG Ausgabe vom 22. Oktober 2020*", wl boersen ausl d.pdf.
[46] Art.26 lit. a.- c. FinfraG.

venues represents a major difference to EMIR. As a consequence, a large industrial group may be a small non-financial entity in Switzerland but a NFC+ in the EU.

ii) Commodity derivatives for physical settlement

Further, for in contrast to the broader general definition of derivatives as per (i) above, in particular **commodity derivatives** are exempt from the clearing regulation under the following prerequisites[47]:

aa) they must be physically delivered,

bb) they cannot be settled in cash at a party's discretion, and

cc) are not traded on a trading venue or an organized trading facility.

The term organized trading facility is defined under Art. 42 FinfraG i.a. as an establishment for

- the multilateral trading in securities or other financial instruments whose purpose is the exchange of bids and the conclusion of contracts based on **discretionary rules**[48]; or
- multilateral trading in financial instruments other than securities whose purpose is the exchange of bids and the conclusion of contracts based on **non-discretionary rules**[49];

The Swiss OTF regulation under the FinfraG refers to Swiss incorporated entities only[50]. Non-Swiss-OTFs, for example such within the EU, do not require formal acknowledgement under Swiss law, in particular not regarding the classification of its products nor in order to allow market access for Swiss counterparties[51]. As

[47] Art. 94 (3) lit. c FinfraG.
[48] Art. 42 lit. a FinfraG.
[49] Art. 42 lit b FinfraG.
[50] The same way as the EU-OTF refers to EU-regulated entities only.
[51] FINMA circular 01/2016, FINMA-Aufsichtsmitteilung 01/2016 Finanzmarktinfrastrukturgesetz: Nächste Schritte der FINMA, no. 4, organized trading facilities, page 9, 20160707 FINMA Aufsichtsmitteilung 01 2016 (1).pdf

a consequence, all physically settled commodity derivatives traded at an EU-OTF including but not limited to those which fall under the REMIT carve-out are exempt from the clearing rules as these instruments must be physically settled and do not fall under the definition of either venue traded or OTF-traded as per Art. 94 (3) lit. c FinfraG.

iii) Determination of small counterparties

The clearing mandate only applies to transactions where none of the contractual parties is a **small counterparty** which is determined against the applicable threshold. A small non-financial counterparty[52] has insofar to stay below a value of **3.3 bn CHF**[53] average gross positions in outstanding and non-privileged OTC commodity derivatives transactions.

iv) Hedging:

For a non-financial counterparty, derivatives transactions intended to reduce risks are not factored into the calculation of the average gross position if they are directly associated with the business activity, liquidity management or asset management of the counterparty or group[54].

The notion of risk reducing is further detailed in Art. 87 FinfraV[55]. Macro-, proxy- and portfolio-hedging is explicitly recognized.

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[52] Art. 98 FinfraG
Kleine Nichtfinanzielle Gegenparteien
1 Eine Nichtfinanzielle Gegenpartei gilt als klein, wenn alle ihre über 30 Arbeitstage berechneten gleitenden Durchschnittsbruttopositionen in den massgebenden ausstehenden OTC-Derivatgeschäften unter den Schwellenwerten liegen.
2 Übersteigt eine der nach Absatz 1 berechneten Durchschnittsbruttopositionen einer bestehenden kleinen Nichtfinanziellen Gegenpartei den massgebenden Schwellenwert, so gilt diese Gegenpartei nach vier Monaten ab dem Zeitpunkt des Übersteigens nicht mehr als klein.
3 Für die Berechnung der Durchschnittsbruttoposition werden Derivatgeschäfte zur Reduzierung von Risiken nicht einberechnet, wenn sie unmittelbar mit der Geschäftstätigkeit oder der Liquiditäts- oder Vermögensbewirtschaftung der Gegenpartei oder der Gruppe verbunden sind.
[53] Art. 88 lit. e. FinfraV.
[54] Art. 98 (3) FinfraG.
[55] Art.87 lit. a - d FinfraV.

v) Intra-group transactions and global reach:

- If the counterparty is part of a fully consolidated group, all of the intra-group OTC derivatives transactions concluded by the counterparty or by other counterparties shall also be factored into the calculation of the average gross positions[56].

- Like EMIR, the FinfraG considers all transactions of fully consolidated group entities for the threshold calculation of the Swiss based in-scope entity, provided, such group entity would be considered as either financial or non-financial counterparty if it was based in Switzerland[57].

vi) Voluntary cleared positions:

Voluntary cleared positions have to be factored into the calculation as well[58].

vii) Netting:

The netting of opposing positions in derivatives is permitted insofar as these positions relate to the same underlying instrument, are denominated in the same currency and have the same maturity date. In such case, the reference interest rates for variable-interest positions, the fixed interest rates and the interest-setting reference dates must be identical[59].

[56] Art. 100 (3) FinfraG.
[57] Art. 89 lit. c FinfraV: „*Positionen von vollkonsolidierten Gruppengesellschaften, einschliesslich derjenigen mit Sitz ausserhalb der Schweiz, werden unabhängig vom Sitz der Muttergesellschaft einberechnet, wenn diese Gruppengesellschaften in der Schweiz als Finanzielle oder Nichtfinanzielle Gegenpartei gelten würden.*“
[58] Art. 88 lit.b FinfraV.
[59] Art.88 lit.f FinfraV.

We visualize the joint features and differences of the Swiss and the EU-model in the following table:

Table 3 – Commodity trading and the clearing obligation (based on the EU Model)

	EU (EMIR)	SUI (FinfraG)
I. Purpose and scope	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)	Reducing of systemic risk by mandatory clearing. Determination of market participants relevant for the clearing mandate (Pittsburgh commitments)
1. Threshold Amount	3 bn EUR - per group -	3.3 bn CHF - per group -
2. In-scope entities	All entities, including non-financial entities and end-users	All entities including non-financial entities and end-users
3. In-scope activities	Any trading activity	Any trading activity
4. In-scope products	"OTC-Derivatives"	"OTC-Derivatives", excluding all instruments traded at trading venues incl. MTFs
a) includes physically settled products	Yes	Yes, partly, but limited to Swiss OTFs, others not considered derivatives
b) includes physically settled ETD on third country venues	Yes if venue not individually recognized as equivalent	No, because not considered OTC or not considered derivatives
c) includes financially settled ETD on third country venues	Yes, if venue not individually recognized as equivalent	No, because not considered OTC

	EU (EMIR)	SUI (FinfraG)
5. Geographical coverage	Global reach for all in-scope instruments and activities	Global reach, except third country venues
a) third country business of affiliates in scope	Yes	Yes
6. Includes intra-group transactions	Yes	Yes
7. Privileged transactions not counting against threshold	Yes	Yes
a) Hedging	Yes, if objectively measurable as reducing risks relating to entity's commercial activity	Yes, if objectively measurable as reducing risks relating to entity's commercial activity
i) Hedging on portfolio level / macro hedging	Yes	Yes
ii) third party commercial positions eligible for hedging	No	No
b) netting effects recognized	Yes, limited	Yes, limited
II.1. Threshold amount and reference	3 bn EUR commodity threshold -per group -	3.3 bn CHF commodity threshold for non-financials/ 8 bn CHF general threshold for financials - per group -
II.2. Reference period for calculation	Every 12 months as aggregate month-end average position for the previous 12 months	Rolling 30-days gross average in open positions

[table 3 comparison EMIR/FinfraG contd.]

As a conclusion, we see that even within the EMIR-concept, there are options to follow a more lenient approach, in particular with a view towards in-scope products and third country venues.

In summary, the Swiss system is largely comparable to the EMIR system**, albeit the treatment of venue traded and physical instruments is more lenient compared to EMIR.**

- **MTF transactions do not count as OTC-Derivatives**
- **Third country trading venues, including exchanges and MTFs, do not require formal recognition in order not deemed to be OTC-markets.**
- **Physically settled third country commodity derivatives drop out of scope as either privileged physical products or not deemed to be OTC-products.**

II. US – Dodd-Frank-Act

We compare the US approach under the US Dodd-Frank-Act ("**DFA**")[60] as transposed inter alia into the Commodity Exchange Act (**CEA**[61]) in the form of the rules and announcements of the Commodity Futures Trading Commission ("**CFTC**") issued in this regard.

1. General: Swap Dealer Test under the DFA: A qualitative concept with quantitative elements

(a) The regulation of commodity trading entities under the DFA with regard to the clearing mandate starts with determining a qualitative basis. The DFA only provides oversight of entities and require clearing if such entities are:

- engaged in financially settled swap transactions and
- performing dealer type activities as regular business.

(b) Only for the limited subset of entities engaged in commodity trading activities that meet this description (either referred to as potential Swap Dealers (**SD**) or potential Major Swap Participant (**MSP**), the quantitative threshold becomes relevant. Almost all registered SDs are major financial service providers (e.g. Morgan Stanley, Goldman Sachs, Deutsche Bank, Unicredit, BNP Paribas).[62]

(c) The quantitative threshold of USD 8 Billion[63] is only relevant as the **final step** of the analysis **after** the swap dealing activities have been established. It exists as a *de minimis fallback* to distinguish system relevant from not system relevant swap dealing entities. This threshold, because of the qualitative aspects tested before, does in essence separate smaller from larger financial service firms. Its ultimate purpose consists to a lesser extent in separating financial service firms from real

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[60] Dodd-Frank Wall Street Reform and Consumer Protection Act of January 5, 2010; available at https://www.cftc.gov/sites/default/files/idc/groups/public/@swaps/documents/file/hr4173_enrolledbill.pdf.
[61] 7 US Code Chapter 1, see at 7 U.S. Code Chapter 1 - COMMODITY EXCHANGES | U.S. Code | US Law | LII / Legal Information Institute (cornell.edu).
[62] See under https://www.nfa.futures.org/registration-membership/membership-and-directories.html, Currently (23 August 2021) 109 qualifying entities registered, almost exclusively financial institutions (all apart from BP, Shell and Mitsui).
[63] Uniform single threshold, not split up per asset class.

economy firms because this is achieved by singling out hedging activities at step one before. Thus, the functional EU equivalent is more the FC+ and FC- distinction in EMIR rather than the separation of NFC- from NFC+. As a consequence, crossing the clearing threshold and qualifying as a Swap Dealer prompts a number of additional obligations comparable to those applying under MiFID II to investment firms[64] and go beyond the EMIR-obligations for a NFC+.

The CFTC describes the self-assessment process as follows[65]:

- The person would begin by applying the statutory definition, and the provisions of the rule which implement the four statutory tests and the exclusion for swap activities that are not part of "a regular business" in order to determine if the person is **engaged** in **swap dealing activity**.
- if, after completing this review (taking into account the applicable interpretive guidance and excluding any swaps as noted above), the person determines that it is engaged in swap dealing activity, the next step is to determine if the person is engaged in **more than a de minimis quantity of swap dealing**. If so, the person is a Swap Dealer.

2. In-scope activities

The US regulation is applicable to **dealing activities only**. Trading (on own account) is distinct from dealing and only in scope for the Swap Dealer test under additional qualifying prerequisites. Generally, a trader trades in his own interest, while a dealer deals in the interest and/or account of a third party[66]. This third party might be the customer or the counterparty of the dealer.

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[64] See final rule on Capital Requirements of Swap Dealers and Major Swap Participants, 2020-16492a.pdf (cftc.gov).
[65] Page 48-49 of the joint SEC-CFTC guidance: Final Rule: Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant."
[66] For a detailed definition of the term "dealer", see CFTC (joint rulemaking with SEC), Final Rule Regarding Further Defining "Swap Dealer", "Major Swap Participant" and "Eligible Contract Participant", 77 Fed. Reg. 30595 (May 23, 2012), p. 30607 et seqq.; available at: https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2012-10562a.pdf.

The details under CEA §1 a(49) are stipulated as follows:

(1) The term swap dealer means any person who:

(i) Holds itself out as a dealer in swaps;

(ii) Makes a market in swaps;

(iii) Regularly enters into swaps with counterparties as an ordinary course of business for its own account; ***or***

(iv) Engages in any activity causing it to be commonly known in the trade as a dealer or market maker in swaps.

Own account trading activity as captured under (iii) above is therefore only in scope if it can be characterized as ordinary course of business which, according to the CFTC-rules[67] require:

(i) Entering into swaps with the purpose of satisfying the **business or risk management needs of the counterparty** (as opposed to entering into swaps to accommodate one's own demand or desire to participate in a particular market);

(ii) maintaining a **separate profit and loss statement** reflecting the results of swap activity or treating swap activity as a separate profit center; or

(iii) having staff and resources allocated to dealer-type activities with counterparties, including activities relating to credit analysis, customer onboarding, document negotiation, confirmation generation, requests for novations and amendments, exposure monitoring and collateral calls, covenant monitoring, and reconciliation.

Any one of these indicators may be sufficient, based on a facts and circumstances analysis, to reach a conclusion that an entity is engaged in "a regular business" of entering into swaps."

[67] Page 64 Final Rule: Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant."

As a consequence, the broad majority of EU-type non-financial counterparties (or *commercial end users* in the US-terminology) are out of scope of the Swap Dealer test from the beginning as they do neither deal for third parties, nor maintain a separate P&L for own account swap trading or have staff and resources allocated to dealer-type activities. In fact, broadly speaking, only those market participants which maintain own proprietary trading activities or trade as service for others are potential swap dealers.

For that very reason, the discussion about the right level of the de minimis clearing threshold is to a large extend held with a view to maintain a significant number of smaller Swap Dealers available **as counterparties for the benefit of end-users**, in particular to hedge and mitigate their business risk as opposed to focus on the activity and status of the end-user at all[68].

Contrary to that, as of now, the discussion about the appropriate EMIR-threshold for the distinction of NFC+ and NFC- did not consider the headroom needed for traders **offering** hedges to third parties but rather limited the space for those entities **requiring** the hedges.

By comparing the legal approach towards such activities, it has to be noted that EU-law, even if it does not incorporate the dealing/trading distinction in a general way which both are considered financial activities[69], it does in fact legally recognize its differences. For example, the ancillary activity exemption in Art. 2 (1) lit. j MiFID II introduces a difference between simple own account trading and own account dealing for third parties, in particular dealing on own account when executing client orders[70].This possible differentiation though is not used or reflected by EMIR.

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[68] Federal Register 83 FR 27444 06/12/2018 De Minimis Exception to the Swap Dealer Definition *"The Commission believes that a $3 billion AGNA de minimis threshold could lead certain entities to reduce or cease swap dealing activity to avoid registration and its related costs. Generally, the costs associated with registering as an SD may exceed the revenue from dealing swaps for many small or mid-sized banks and non-financial entities. Additionally, some persons engaged in swap dealing activities below the current $8 billion threshold have indicated that swap dealing is not a major source of revenue and is only complementary to other client-facing businesses, suggesting that these smaller dealing entities could reduce or eliminate their swap dealing activities if the threshold is lowered. Although the magnitude of this effect is not certain, reduced swap dealing activity could lead to increased concentration in the swap dealing market, reduced availability of potential swap counterparties, reduced liquidity, increased volatility, higher fees, wider bid/ask spreads, or reduced competitive pricing.* ***The end-user counterparties of these smaller swap dealing entities may be adversely impacted by the above consequences and could face a reduced ability to use swaps to manage their business risks****".*

[69] A(3) Annex I MiFID II.

[70] See also differentiation in German law: *Eigenhandel* vs. *Eigengeschäft* in § 32 KWG and § 2 KWG.

To summarise, because of the US dealer-trader distinction, many activities covered by EMIR due to the "product-only approach", are out of scope in the first place with regard to the DFA as they do not constitute "*dealing*" on a qualitative level.

3. In-scope entities and coverage

As explained above, hedging own commercial risk with a swap is not a dealing activity – opposed to hedging commercial risk for the counterparty of that swap. Therefore entities which only trade for own commercial risk mitigation purposes drop out of the definition.

Consequently, **commercial end users** which are not financial entities[71], for example not meeting the Swap Dealer test, are explicitly exempt from clearing if they avail themselves to the end user exception. [72]

From an entity or market participant perspective, the dealer-trader distinction and the privilege for commercial end users effect, that most non-financial trading entities are fully out of scope of the DFA definition of a potential Swap Dealer[73] as they do not engage in any dealing activity nor trade own account under a separate profit center.

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[71] See financial entity definition under section 2 (h) (7) (C) of the CEA, 7 U.S. Code § 2 - Jurisdiction of Commission; liability of principal for act of agent; Commodity Futures Trading Commission; transaction in interstate commerce | U.S. Code | US Law | LII / Legal Information Institute (cornell.edu).

[72] *Non-financial entities (1) A counterparty to a swap may elect the exception to the clearing requirement under section 2(h)(7)(A) of the Act if the counterparty:*
(i) Is not a "financial entity" as defined in section 2(h)(7)(C)(i) of the Act;
(ii) Is using the swap to hedge or mitigate commercial risk as provided in paragraph (c) of this section; and
(iii) Provides, or causes to be provided, the information specified in paragraph (b) of this section to a registered swap data repository or, if no registered swap data repository is available to receive the information from the reporting counterparty, to the Commission. A counterparty that satisfies the criteria in this paragraph (a)(1) and elects the exception is an "electing counterparty."
See also final rule on end user exemption 2012-17291.pdf (govinfo.gov). Commercial End User must meet notification and reporting requirements towards the CFTC when it elects to avail itself of the Commercial End-User-Exemption. However, the CFTC permits the electing counterparty to report the required information on an annual basis, thereby significantly reducing costs and efforts; for further details see Code of Federal Regulations, Title 17, Chapter I (17 CFR), Part 50; §50.50(b); available at https://www.law.cornell.edu/cfr/text/17/50.50.

[73] 17 CFR § 1.3, (definitions): "The term swap dealer does not include a person that enters into swaps for such person's own account, either individually or in a fiduciary capacity, but not as a part of regular business.

4. In-scope products

The Dodd-Frank Act clearing mandate applies to **swaps** as defined in section 1a (47) CEA which does in general **not** include **physically settled products**[74]. Transactions for physical delivery of commodities including those intended to be **physically settled** are **not** swaps:

The Term "swap" does not include:

(i)

Any contract of sale of a commodity for future delivery (or option on such a contract), leverage contract authorized under section 23 of this title, security futures product, or agreement, contract, or transaction described in section 2(c)(2)(C)(i) of this title or section 2(c)(2)(D)(i) of this title;

(ii)

any sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled;

a) Forward Contract Exclusion

As a consequence, the Swap Dealer concept does not apply to physically settled bilateral commodity forwards[75] in the first place, irrespective of its ultimate commercial purpose as long as such commodity forward was intended[76] to be physically settled and irrespective of its place of execution. Under this prerequisites, embedded physical

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[74] See (lengthy) Section 1a(47) of the CEA; available at 7 U.S. Code § 1a - Definitions | U.S. Code | US Law | LII / Legal Information Institute (cornell.edu) as added by Section 721(a) of the Dodd-Frank Act, including for example interest rate swaps and currency swaps, commodity swaps and options based on interest or a currency exchange rates or commodities.

[75] See Section 1a(47)(B)(ii) of the CEA and CFTC (joint rulemaking with SEC), Final Rule Regarding Further Definition of ''Swap,'' ''Security-Based Swap,'' and ''Security-Based Swap Agreement''; Mixed Swaps; Security-Based Swap Agreement Recordkeeping 77 Fed. Reg. 48207 (August 13, 2012), p. 48227 et seqq, so-called **forward contract exclusion**; available at https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2012-18003a.pdf.

[76] In assessing the parties' expectations or intent regarding delivery, the CFTC consistently has applied a ''facts and circumstances'' test, taking into account the contractual provisions and the industry practices at the market in question. The CFTC reads the ''intended to be physically settled'' language in the swap definition with respect to nonfinancial commodities to reflect a directive that intent to deliver a physical commodity be a part of the analysis of whether a given contract is a forward contract or a swap, just as it is a part of the CFTC's analysis of whether a given contract is a forward contract or a futures contract, as above, 77 Fed. Reg. (August 13, 2012, p. 48228.

options[77] and forwards on intangible commodities such as environmental products[78] are excluded as well.

b) Exclusion of Futures

Furthermore, the definition of swap under Title VII of the DFA is largely limited to bilateral transactions[79] and excludes from its scope the trading of listed commodity **futures** at exchanges with the exchange as central counterparty.

c) Other exclusions

Pursuant to various CFTC regulations, certain swaps, subject to specific conditions, do not have to be considered in determining whether a person is a Swap Dealer, e.g. including swaps between affiliates[80] and swaps hedging own physical positions[81].

We discuss these in more detail under the *threshold calculation methodology*, section 5 below but as interim result we note that - **in addition** to addressing a much smaller number of in-scope entities – the product scope covered by the DFA is **also significantly more narrow** than under EMIR.

5. Threshold calculation methodology

a) Threshold amount

For market participants currently not registered as Swap Dealers or Major Swap Participants but who would, as a result of their swap dealing activity, in principle be covered under the DFA, there is a quantitative clearing threshold in the form of the ***de minimis exception*** pursuant to Section 1a (49)(D) of the CEA[82].

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[77] As above, see *Commodity Options Embedded in Forward Contracts*, Federal Register / Vol. 77, No. 156 / Monday, August 13, 2012 / Rules and Regulations 48237.
[78] As above, Federal Register / Vol. 77, No. 156 / Monday, August 13, 2012 / Rules and Regulations p. 48233.
[79] See *Distinguishing Futures and Options From Swaps*, Federal Register / Vol. 77, No. 156 / Monday, August 13, 2012 / Rules and Regulations p. 48303, further see Section 1a(47) of the CEA and the CFTC No-Action Letter Regarding Certain Conditions of the Floor Trader Provision, June 27, 2019 , available at https://www.cftc.gov/system/files/csl/final/pdfs/19/1561667900/19-14.pdf.
[80] See 17 CFR § 1.3 (ggg)(6)(i) available at 17 CFR § 1.3 - Definitions. | CFR | US Law | LII / Legal Information Institute (cornell.edu).
[81] See 17 CFR § 1.3 (ggg)(6)(iii), as above.
[82] Further specified in 17 CFR § 1.3 (ggg)(4), as above.

It states that a person shall not be deemed to be a Swap Dealer unless its swaps connected with swap dealing activities exceed an aggregate gross notional amount ("**AGNA"**) threshold of **$8 billion**[83]. As a consequence, only a very limited number of market participants qualify as Swap Dealers[84]. With regard to the second category of regulated traders, the **Major Swap Participant**, the definition is even narrower[85] and the outturn correspondingly **extremely low**[86].

This threshold only applies to **the in-scope products** as defined above:

Its definition states in full:

> ***"De minimis exception****- (i)(A)In general. Except as provided in paragraph (4)(vi) of this definition, a person that is not currently registered as a swap dealer shall be deemed not to be a swap dealer as a result of* ***its swap dealing activity*** *involving counterparties, so long as* ***the swaps connected with those dealing activities*** *into which the person - or any other entity controlling, controlled by or under common control with the person - enters over the course of the immediately preceding 12 months have an aggregate gross notional amount of no more than* ***$8 billion****, and an aggregate gross notional amount of no more than $25 million with regard to swaps in which the counterparty is a "special entity" (as that term is defined in section 4s(h)(2)(C) of the Act, 7 U.S.C. 6s(h)(2)(C), and § 23.401(c) of this chapter), except as provided in paragraph (4)(i)(B) of this definition. For purposes of this definition, if*

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[83] 17 CFR § 1.3 (ggg)(4) (i)(A) for the rationale see CFTC Final Rule Regarding De Minimis Exception to the Swap Dealer Definition, 83 Fed. Reg. 56666 (November 13, 2018), p. 56677; available at https://www.cftc.gov/sites/default/files/2018-11/2018-24579a.pdf. The envisaged lowering of the threshold down to 3 billion USD was dismissed with various arguments including to prevent from 1) Increased concentration in the swap dealing market; (2) reduced availability of potential swap counterparties; (3) reduced liquidity; (4) increased volatility; (5) increased systemic risk; and/or (6) higher fees or reduced competitive pricing. The CFTC was rather of the opinion that the current 8 billion serves the regulatory purpose well and leaves sufficient headroom to dealing to the benefit of commercial end users.

[84] In 2012 the CFTC delegated the registration of Swap Dealers to the National Futures Association ("NFA"). See CFTC Notice and Order regarding Performance of Registration Functions by National Futures Association With Respect To Swap Dealers and Major Swap Participants 77 Fed.Reg 2708 (January 19, 2012); According to the NFA's Swap Dealer Registry (available at https://www.nfa.futures.org/registration-membership/membership-and-directories.html), as of 23 August 2021, 109 entities were registered with the NFA, often listing several subsidiaries, particularly of large financial companies (e.g. Goldman Sachs, Merrill Lynch and Morgan Stanley); additionally, the CFTC provides a list with provisionally registered Swap Dealers; available at https://www.cftc.gov/LawRegulation/DoddFrankAct/registerswapdealer.html.

[85] See 17 CFR § 1.3 and CFTC Final Rule, 77 Fed. Reg. 30595 (May 23 2012), p.30661 et seqq. (IV.).

[86] As of 23 August 2021, there were **no entities** registered as a Major Swap Participant with the NFA. https://www.nfa.futures.org/registration-membership/membership-and-directories.html.

the stated notional amount of a swap is leveraged or enhanced by the structure of the swap, the calculation shall be based on the effective notional amount of the swap rather than on the stated notional amount"[87].

b) Reference period

Generally, an entity must count towards its AGNA threshold all swaps it entered into for **dealing purposes** over the **preceding 12 months**. Thus, to the extent that a particular swap or security-based swap is not connected to dealing activity, it will not count against the de minimis thresholds. Conversely, if a swap is connected to the person's dealing activity, the position will count against those thresholds[88].

In addition, unlike under EMIR, where the annual calculation usually takes place from June until June the following year, only swaps that have been **entered into** in the **previous 12 months** count against the threshold. Therefore, swaps entered into for a period of more than a year will **drop out** on a rolling basis. Any double or multiple counting of existing swaps and the respective open positions – as under EMIR – is avoided. In fact, the threshold under the Dodd-Frank measures the **dealing activity** of a person rather than the size of actual open positions.

c) Geographical coverage – third country business of affiliates

According to Section 2 (i) of the CEA, the swap provisions of the CEA apply to cross-border activities when certain conditions are met, namely, when swap dealing activities have a "**direct and significant connection with activities in, or effect on, commerce of the United States**[89]**"** or when they contravene Commission rules or regulations as are

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[87] 17 CFR § 1.3 - Definitions. | CFR | US Law | LII / Legal Information Institute (cornell.edu).

[88] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30631.

[89] "*The Commission believes that section 2(i) provides it express authority over swap activities outside the United States when certain conditions are met, but it does not require the Commission to extend its reach to the outer bounds of that authorization. Rather, in exercising its authority with respect to swap activities outside the United States, the Commission will be guided by international comity principles and will focus its authority* ***on potential significant risks to the U.S. financial system"****, see 56928 Federal Register / Vol. 85, No. 178 / Monday, September 14, 2020 / Rules and Regulations.*

necessary or appropriate to prevent evasion of the swaps provisions[90] of the CEA enacted under Title VII of the DFA.

Activities without such connection to US-commerce or not deemed to circumvent swap provisions are not in scope of the regulation if the swap trading activity is performed by non-US group entities of the (actual or) potential swap dealer.

i) As a starting point, each US-person[91] engaged in swap dealing activities calculates the AGNA of its entire **own** swap dealing activity[92]. Whether the swap is executed abroad with a third party counterparty or entered into by a foreign branch of the US-person does not release the person from including such transaction into its calculation. If exceeding the threshold, the person is a swap dealer.

ii) Secondly, each person whose own swaps do not yet exceed the AGNA threshold must – in principle but limited by the exemption discussed below - also include in its de minimis calculation the AGNA of swaps of any other unregistered affiliate, i.e. affiliates not registered as Swap Dealer or Major Swap Participant, controlling, controlled by, or under common control with that person (so-called ‘‘**aggregation**’’)[93]. The term ‘‘affiliates under common control’’ in this context includes parent companies and subsidiaries, and is not limited to ‘‘sister companies’’ at the same organizational level[94].

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[90] As for example by booking strategies such as deliberately arranging swaps with US-market underlying or US-exchange price references between third country entities of US-groups to be settled outside the US.
[91] the term ‘‘U.S. person’’ encompasses a person that, by virtue of being domiciled, organized, or having its principal place of business in the United States, raises the concerns intended to be addressed by the Dodd-Frank Act, regardless of the U.S. person status of its counterparty. In addition, a person’s status as a U.S. person is determined at the entity level and, thus, a U.S. person includes the swap dealing activity of operations that are part of the same legal person, including those of its foreign branches. Therefore, a U.S. person includes in its SD de minimis threshold calculation dealing swaps entered into by a foreign branch of the U.S. person, See definition at CFTC Final Rule, 85 Fed .Reg. 56924 (September 14, 2020), p. 56932; mostly corresponding with definition in CFTC Guidance, 78 Fed. Reg. 45291 (July 26, 2013).
[92] 17 CFR § 23.23(c)(1).
[93] 17 CFR § 1.3(ggg)(4)(1); CFTC Final Rule, 83 Fed .Reg. 56666 (November 13, 2018), p. 56679.
[94] CFTC Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 Fed. Reg. 45291 (July 26, 2013), p. 45323, footnote 308; available at https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf.

iii) Such affiliates may either be **US persons**, in particular if they are incorporated in the US or **non-US persons**, if incorporated abroad. The CFTC applies the same aggregation principles to all affiliates in a corporate group, irrespective of whether they are US or non-US persons[95] but unlike US-persons, non US-persons do not need to consider all swap dealing activities. Both US and non-US persons in an affiliated group may engage in swap dealing activity up to the de minimis threshold

iv) When the affiliated group meets the de minimis threshold in aggregate, one or more affiliate(s) (inside or outside the United States) would generally have to register as Swap Dealer(s) so that the relevant swap dealing activity of the unregistered affiliates remains below the threshold.

v) As indicated above, unlike US-persons, not all swap dealing activity of affiliated non US-persons have to be considered for the threshold calculation in the same manner. Instead, whether a non-US person is required to include its swap dealings and/or the swap dealings of its affiliates into its de minimis threshold calculations requires an **impact on the stability of US-markets** and will therefore depend on **additional criteria** regarding its status, the status of its counterparty, and the jurisdiction in which it is regulated. These criteria haven been recently defined and introduced by a new final rule[96] as of November 2020, published by the CFTC and superseding the 2013 so-called Cross-border Guidance[97].

In essence, a non-US person only has to calculate all its swap dealing activity if it qualifies as a "Guaranteed Entity" or "significant risk subsidiary" ("**SRS**")[98]. Both

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[95] CFTC Final Rule Regarding Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, 85 Fed. Reg. 56924 (September 14, 2020); available at https://www.cftc.gov/sites/default/files/2020/09/2020-16489a.pdf; p. 56951.

[96] CFTC Final Rule Regarding Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, 85 Fed. Reg. 56924 (September 14, 2020); available at https://www.cftc.gov/sites/default/files/2020/09/2020-16489a.pdf;; for an overview of all changes to CFTC Regulation Section 23.23, see p 56997 et seqq.

[97] CFTC Guidance, 78 Fed. Reg. 45291 (July 26, 2013).

[98] See definitions at CFTC Final Rule, 85 Fed. Reg. 56924 (September 14, 2020), p. 56941 et seq.:
A "Guaranteed Entity" is a non-U.S. person whose swaps are guaranteed by a U.S. person, with respect to those swaps that are so guaranteed. A "significant risk subsidiary" is any non-U.S. significant subsidiary of an ultimate U.S. parent entity where the ultimate

new introduced categories of market participant serve as a proxy to identify such entity which present a risk exposure to the US-markets and differentiate these from other affiliated non-US-persons.

vi) Any "other Non-US person", however, is generally only required to count swap dealings with another US person towards its de minimis threshold, except for swaps conducted through a foreign branch[99] of a registered US Swap Dealer and — subject to certain exceptions — also swap dealing if its counterparty is a Guaranteed Entity[100].

Therefore, swaps entered into by other Non-US persons do not count towards the de minimis thresholds – neither their own nor if its affiliated US-group entities, as long as no US person or Guaranteed Entity is involved as counterparty.

This limitation presents a **significant difference to the EU-approach** under EMIR as EMIR considers all group affiliated OTC-derivative transactions even executed in third countries without any comparable test on the impact on the EU-market. The categories of "guaranteed entities" and "SRS" are introduced to determine exactly such potential impact to the US-market by using guarantees and the exposure to the US-group as indications for such nexus[101].

In addition, an "other Non-US person" may also exclude from its de minimis threshold any swap that it entered into on a designated contract market, a swap execution facility registered with the CFTC or exempted by the CFTC from registration, or a foreign board of trade ("**FBOT[102]**") registered with the CFTC, if the swap is also cleared through a registered or exempt derivatives clearing organization and where the non-US-person does not know

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U.S. parent entity has more than $50 billion in global consolidated assets, as determined in accordance with U.S. GAAP at the end of the most recently completed fiscal year, with certain exceptions.

[99] See in detail CFTC Final Rule, 85 Fed. Reg. 56924 (September 14, 2020), p.56947.

[100] 17 CFR § 23.23(c)(2).

[101] "*In this way, non-U.S. persons receiving support from a U.S. person and representing a significant risk to the U.S. financial system are captured by the Final Rule. Accordingly, the Final Rule achieves the dual goals of protecting the U.S. markets and promoting a workable cross-border framework*.", CFTC Final Rule, 85 Fed. Reg. 56924 (September 14, 2020), p.56941.

[102] There are currently 23 FBOTs registered with the CFTC, including Commodity Exchanges such as European Energy Exchange, Dubai Mercantile Exchange, ICE Futures Europe, ICE-Endex, The London Metal Exchange, NASDAQ Oslo ASA and the Tokyo Commodity Exchange[102]. It has to be noted, however, that such registration is primarily done in order to qualify for direct access to this venue from the US and less so, to obtain a privileged status for the Swap Dealer test. In fact, a very limited number of products traded at these FBOTS would at all qualify as Swaps instead of Futures.

the identity of the counterparty prior to execution[103] as it could not assess the impact of the transaction on its clearing threshold usage absent such information. This exclusion, however, comes on top of any other provision of the Cross Border Rule and does not relate to exchange traded futures which are out of scope of the SD determination from the beginning.

Since the question of which swaps dealing activities are included in the de minimis threshold depends on personal criteria, predominantly on whether US persons are involved or US markets impacted, it is less relevant whether the swap traded by an US-person is executed in the US or in a third country. Non US-incorporated affiliates of US persons, however, not qualifying as “SRS” or “guaranteed entity” and which trade swaps on foreign venues would **not include** such transaction into the threshold calculation and thereby not affecting their group clearing threshold.

[103] CFTC Final Rule, 85 Fed. Reg. 56924 (September 14, 2020), p. 56956, 56999, 17 CFR § 23.23(d).

The result had been visualized by the CFTC as follows[104]:

Counterparty → / Potential SD ↓		U.S. Person	Non-U.S. Person		
			Guaranteed Entity	SRS	Other Non-U.S. Person
U.S. Person		Include	Include	Include	Include
Non-U.S. Person	Guaranteed Entity	Include	Include	Include	Include
	SRS	Include	Include	Include	Include
	Other Non-U.S. Person[1]	Include[2]	Include[3]	Exclude	Exclude

[1] Does not include swaps entered into anonymously on a DCM, a registered SEF or a SEF exempted from registration, or a registered FBOT and cleared through a registered DCO or a DCO exempted from registration.
[2] Unless the swap is conducted through a foreign branch of a registered SD.
[3] Unless the Guaranteed Entity is registered as an SD, unless the guarantor is a non-financial entity, or unless the Guaranteed Entity is itself below the de minimis threshold and is affiliated with a registered SD.

In this respect, there is a **notable difference** to the EU's approach, which focuses on the type of instrument and market at which the transaction is executed, regardless whether by EU or non EU-persons.

For comparison:

- a Swap transaction **in the EU** between two EU-incorporated entities belonging to US-groups would not count against the DFA-threshold but would do so against the EMIR-threshold,

[104]Final rule *Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants,* Table A, p.56994, 2020-16489a.pdf (cftc.gov).

- a Swap transaction **in the US** between two US-incorporated entities belonging to EU-groups would count against the DFA-threshold **but also** against the EMIR-threshold.

  The latter would even be the case if such transaction would be neglected for the DFA-assessment because it may not constitute dealing or the product is for physical settlement.

As consequence, transactions performed at the US market might be considered irrelevant for the Swap Dealer Test and US-regulation, but would still and at the same time be viewed relevant for the EU-market, even if no EU-product, EU-venue or EU-entity involved.

As a conclusion, the EU-approach is universal and leads to much higher values since any OTC-derivative transaction of any group company contributes to the group's threshold consummation. Contrary thereto, the US law has developed certain criteria to differentiate between transactions, which may impact the US-market and those, which would not. The latter are out of scope for further assessment.

d) Exclusion of intra-group transactions

Inter-affiliate activities, i.e. swaps between majority-owned affiliates, shall **not** be included into de minimis threshold calculation[105].

> **(6)** ***Swaps that are not considered in determining whether a person is a swap dealer***
>
> **(i)** ***Inter-affiliate activities.*** *In determining whether a person is a swap dealer, that person's swap with majority-owned affiliates shall not be considered. For these purposes the counterparties to a swap are majority-owned affiliates if one counterparty directly or indirectly owns a majority interest in the other, or if a third party directly or indirectly owns a majority interest in both counterparties to the swap, where majority interest is the right to vote or direct the vote of a majority of a class of voting securities of an entity, the power to sell or direct the sale of a majority of a class of voting*

[105] 17 CFR § 1.3(ggg)(6)(1).

securities of an entity, or the right to receive upon dissolution or the contribution of a majority of the capital of a partnership.[106]

The US regime therefore does not foresee the double counting of inter-affiliate transactions which occur under EMIR (see above).

e) Exclusion of privileged transactions

According to 17 CFR § 1.3(ggg)(6)(iii), swaps entered into for **hedging physical positions** are not considered in the determination of whether a person is a Swap Dealer[107].

The regulation reads:

(iii) *Swaps entered into for the purpose of hedging physical positions.*

In determining whether a person is a swap dealer, a swap that the person enters into shall not be considered, if:

(A) *The person enters into the swap for the purpose of offsetting or mitigating the person's price risks that arise from the potential change in the value of one or several*

(1) *Assets that the person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising;*

(2) *Liabilities that the person owns or anticipates incurring; or*

(3) *Services that the person provides, purchases, or anticipates providing or purchasing;*

(B) *The swap represents a substitute for transactions made or to be made or positions taken or to be taken by the person at a later time in a physical marketing channel;*

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[106] 17 CFR § 1.3 - Definitions. | CFR | US Law | LII / Legal Information Institute (cornell.edu).

[107] In this regard, the statutory definition of the term ‘‘Swap Dealer” stands in contrast to the statutory definition of the term ‘‘Major Swap Participant’’ which explicitly provides that positions in swaps held for hedging or mitigating commercial risk are to be excluded in certain parts of that definition. See CEA Section 1a(33)(A)(i)(1).

> ***(C)*** *The swap is economically appropriate to the reduction of the person's risks in the conduct and management of a commercial enterprise;*
>
> ***(D)*** *The swap is entered into in accordance with sound commercial practices; and*
>
> ***(E)*** *The person does not enter into the swap in connection with activity structured to evade designation as a swap dealer*.

The person must enter into the swap for the purpose of offsetting or mitigating the person's **price risks** that arise from the potential change in the value of one or several assets, liabilities or services and the swap must represent a substitute for transactions made or to be made or positions taken or to be taken by the person at a later time in a physical marketing channel. In addition, the swap has to be economically appropriate to the reduction of the person's risks in the conduct and management of a commercial enterprise and must be entered into in accordance with sound commercial practices[108].

In general, entering into a swap for the purpose of hedging one's own risks is – in the view of the CFTC – inconsistent with swap dealing[109]. According to the CFTC, making a market in swaps is appropriately described as routinely standing ready to enter into swaps at the request or demand of a counterparty, and swap dealing as a ''regular business'' regularly includes entering into swaps to satisfy the business or risk management needs **of the counterparty** as opposed to entering into swaps for the purpose of hedging **one's own risks**. The latter would therefore generally not be indicative of swap dealing[110].

However, the CFTC has not adopted a per se exclusion of swaps for hedging purposes[111]. Rather, the CFTC adopted the ''relevant facts and circumstances'' test established in the Swap Dealer Definition Adopting Release[112] and further discussed in the DSIO FAQ

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[108] See CFR § 1.3(ggg)(6)(iii).
[109] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30611 et seq. and footnote 214; Further Definition of ''Swap Dealer,'' ''Security-Based Swap Dealer,'' ''Major Swap Participant,'' ''Major Security Based Swap Participant'' and ''Eligible Contract Participant'' 2012-10562.pdf (govinfo.gov).
[110] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30611 et seq. and footnote 214.
[111] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30612; see also CFTC Final Rule, 83 Fed. Reg. 56666 (November 13, 2018), p. 56680; there, the CFTC discussed but did not adopt a general hedging exception.
[112] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012).

Guidance 2012[113]. A person must consider the swap in light of all other relevant facts and circumstances to determine whether such hedging activity is swap dealing activity (e.g., accommodating demand for swaps, making a market for swaps, etc.). If hedging or proprietary trading activities do not fulfil the definition, e.g. because of the application of exceptions for hedging physical positions, they do not count against the de minimis thresholds[114].

It is further **not** required that swaps hedge risks on a **one-to-one** transactional basis in order to be excluded, but rather they may hedge on a portfolio basis. The CFTC names swaps that qualify as enumerated hedging transactions and positions as examples of the types of physical commodity swaps that can be excluded from the swap dealer analysis[115]. The swaps qualifying as enumerated hedging transactions and positions are listed in 17 CFR § 151.5(a)(2) and appendix B to part 151[116]. These examples are illustrative of the types of ''assets,'' ''liabilities,'' and ''services'' contemplated in 17 CFR § 1.3(ggg)(6)(iii), because the price risk arising from changes in their value could be offset or mitigated with a swap that represents a substitute for transactions made or to be made or positions taken or to be taken by the person at a later time in a physical marketing channel[117].

f) Netting and off-set of collateral not recognized

The CFTC has explicitly not acknowledged approaches by market participants advocating the possibility of netting or collateral offsets with regard to the de minimis threshold calculations as the possible engaging in large amounts of swap dealing activity while remaining within the de minimis exception, due to that entity netting or collateralizing its swap positions, would – in the CFTC's view – undermine the customer protection and market operation benefits associated with dealer regulation[118].

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[113] DSIO, Frequently Asked Questions (FAQ) – Responds to FAQs About Swap Entities (Oct. 12, 2012), ("DSIO FAQs"); available at https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/swapentities_faq_final.pdf.
[114] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30631 and footnote 433; see also DSIO FAQs, p.2; CFTC Final Rule, 83 Fed. Reg. 56666 (November 13, 2018), p. 56680.
[115] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30612.
[116] 17 CFR § 151.5(a)(2) and appendix B to part 151; available at https://www.law.cornell.edu/cfr/text/17/part-151.
[117] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30612 and footnote 218.
[118] CFTC Final Rule, 77 Fed. Reg. 30595 (May 23, 2012), p. 30630. *Consistent with the proposal, the final rules implementing the de minimis exception take into account the notional amount of an entity's swap or security-based swap positions over the prior 12 months arising from its dealing activity.[422] While the Commissions recognize that notional amounts do not directly measure the*

g) Inclusion of voluntarily cleared derivative contracts

Contracts which are concluded as swaps outside regulated exchanges might nevertheless later assigned to a clearing facility for central clearing. Such voluntary cleared swaps have to be **distinguished from block trades**, which are arranged bilaterally but are only to be registered, executed and cleared at an exchange subject to its rules and therefore no swaps but futures in the first place. Voluntarily cleared swaps, however, have to be included in the calculation of a potential Swap Dealers position, provided the qualitative conditions explained above are fulfilled. The CFTC has taken into consideration the approach to exclude inter alia already cleared swaps from the calculation of the de minimis threshold but has to this date not acted on it[119]. Therefore, voluntarily cleared swaps, if any, stay swaps and also count against the de minimis threshold. However, there are very few cleared swap contracts available at all.

6. Summary

The US-DFA pursues the same regulatory objective as EMIR but deviates in a number of elements:

- The set of in-scope products is significantly smaller as swaps do in general not refer to commodity derivatives for physical settlement nor listed venue traded instruments.
- The in-scope activities are limited to dealing activities and exclude commercial end use of swaps for hedging from the beginning. For that reason, the discussion about

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exposure or risk associated with a swap or security-based swap position, such measures do reflect the relative amount of an entity's dealing activity.[423] Moreover, although some commenters have posited measures of risk or exposure as alternatives to notional measures, such risk or exposure measures could, to the extent they allow for netting or collateral offsets, potentially allow an unregistered entity to engage in large amounts of swap or security-based swap dealing activity while remaining within the de minimis exception so long as that entity nets or collateralizes its swap or security-based swap positions. Such an outcome could undermine the customer protection and market operation benefits associated with dealer regulation. As with the proposed rules, the notional factor in the final rules is based on the notional positions of an entity over a 12 month period, rather than capping the current notional amount of a position at any time, to better reflect the amount of an entity's current activity.

[119] See Swap Dealer De Minimis Exception On-Venue and Cleared Swaps; A Report by Staff of the Division of Swap Dealer and Intermediary Oversight July 2019; available at https://www.cftc.gov/PressRoom/PressReleases/7958-19. See also original statement *In any case, we note that the statutory definition of the term "swap dealer" does not include any factor considering whether the swaps that an entity enters into are cleared as opposed to not cleared*. (Federal Register :: Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant").

the appropriate threshold level does consider the headroom needed for entities **offering** hedges rather than those r**equiring** hedges.

- The geographical coverage does in fact extent beyond US-jurisdiction but is limited to such swap dealing activities which may impact the stability of the US-financial system. In that respect, the US-legislation has developed certain criteria or categories such as guaranteed entity or significant risk subsidiary to differentiate between global activities of US-groups which may impact the US-system und such which do not. The latter are out of scope.

III. Australia

1. General

In Australia, the Pittsburgh summit decisions on the OTC Derivatives market reform have been implemented by a joint effort of the different regulators: The Australian Prudential Regulation Authority (**APRA**), the Australian Securities and Investments Commission (**ASIC**) and the Reserve Bank of Australia (**RBA**).

For commodity trading activities, the relevant regulator is ASIC. The main regulations are the Derivative Transaction Rules (Reporting) 2013[120] and the Derivative Transaction Rules (Clearing) 2015[121]. Both are based on sec. 901A of the Corporations Act (2001)[122]. While the reporting obligations apply to all kind of derivatives, generally including commodity derivatives but excluding electricity derivatives[123], and all kind of trading entities, the applicability of the clearing obligation is both **limited** in **produc**t and **entity scope**.

Only financial entities meeting a threshold of **AUD 100 billion[124]** (Clearing Entity) have to clear their OTC-transactions. The threshold is comparably high but was introduced after careful considerations of its effects[125]. It applies on **entity**, not on group **level** and consequently, each group entity trading derivatives can make use of the applicable threshold separately[126]. The so defined applicability still leads to, roundabout, 20 market participants

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[120] ASIC Derivative Transaction Rules (Reporting) 2013 as amended 2015. (https://www.legislation.gov.au/Details/F2015C00262).
[121] ASIC Derivative Transaction Rules (Clearing) 2015 (https://www.legislation.gov.au/Details/F2015L01960) (**Clearing Rule**).
[122] Corporations Act 2001 as amended (https://www.legislation.gov.au/Details/C2021C00203/Html/Volume_4#_Toc65656546) (**Corporations Act**).
[123] See 1.2.4 Derivative Transaction Rules (Reporting) 2013 with reference to the Corporations (Derivatives) Determination 2013 (http://www.comlaw.gov.au/Details/F2013L00819/30ad4901-5d5e-4ecd-9c2b-ad4b412c45f7) for the definition of OTC derivative and compare Table S.21(2) Derivative Transaction Rules (Reporting) 2013 for required commodity derivative data.
[124] Which equals around 64 bn EURO.
[125] (https://asic.gov.au/media/3252197/cp231-published-28-may-2015.pdf: „*We believe that the proposed clearing threshold of $100 billion gross notional outstanding in OTC derivatives is an appropriate threshold for determining whether an entity should be considered to be an internationally active dealer. These entities will have substantial OTC derivatives exposures and—consistent with the analysis in the July 2013 and April 2014 reports— we believe that the greatest systemic risk reduction will come from including these entities in mandatory central clearing.",* margin 31.
[126] „*We consider it appropriate to apply the clearing threshold to each legal entity, and not at group level. This is consistent with the approach taken in the derivative transaction rules (reporting), and will be the simplest approach for entities to implement. We also propose that the clearing requirements only apply to a legal entity that is above the clearing threshold—and not to its subsidiaries or related entities. Again, we consider this to be the simplest approach for entities to implement, allowing for clear identification of those entities which are clearing entities and those which are not, without needing to determine whether a counterparty is part of a group of entities where the parent entity is at or above the clearing threshold",* as above, margin 38, 39.

having been registered as Clearing Entities[127]. The clearing mandate as such is limited to OTC interest rate derivatives denominated in Australian Dollars, US Dollars, Euros, British Pounds and Japanese Yen.

Therefore, **no non-financial entities trading commodities are affected by the Australian clearing regulation**[128]. Further, third country transactions lacking any nexus to the Australian market, are out of scope of the regulation as well.

However, both the Australian regulators[129] and the Financial Stability Board[130] have established that the Pittsburg commitments have been fully implemented in Australia.

In detail:

2. In-scope entities

Only Clearing Entities are obliged to clear their Clearing Transaction[131] (2.1.1 (1) Clearing Rule). Clearing Entities may be Australian Clearing Entities or Foreign Clearing Entitles. (1.2.4 Clearing Rule). Both have in common that only Financial Entities may qualify as mandatory Clearing Entities[132].

According to 1.2.1 Clearing Rule, Financial Entity means each of the following:

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[127] See at Clearing entity notifications | ASIC - Australian Securities and Investments Commission *Australia New Zealand Banking Group, Bank of America, National Association, ,BNP Paribas, Citigroup Global Markets Limited, Citibank, National Association ,Commonwealth Bank of Australia, Deutsche Bank AG, Goldman Sachs Financial Markets, The Hongkong and Shanghai Bank Corporation (HSBC),JP Morgan ,Chase Bank, N.A, Macquarie Bank Limited, Merrill Lynch International, Morgan Stanley & Co. International plc, National Australia Bank Limited, Nomura Financial Products & Services, Inc., Nomura International plc, Royal Bank of Canada, UBS AG, Westpac Banking Corporation.*

[128] Intended result and rationale further expressed in the explanatory statement in Corporations Amendment (Central Clearing and Single-Sided Reporting) Regulation 2015 (legislation.gov.au): *As mentioned above, this definition, in conjunction with the definition of foreign clearing entity (see below), in effect replicates the scope of the end user exemption in current regulation 7.5A.50 with respect to central clearing. In combination with the level of the threshold it ensures that only major financial institutions are included in the scope of the mandate* (subdivision 2.1.A).

[129] Over-The-Counter Derivatives – Regulatory Framework – Council of Financial Regulators (cfr.gov.au).

[130] FSB, OTC Derivatives Market Reforms, Note on implementation progress for 2020, published on 25 November 2020 (https://www.fsb.org/wp-content/uploads/P251120.pdf), table 1.

[131] As defined by rule 1.2.5. Clearing Rule as a subset of derivatives transactions which qualify for clearing because of a Clearing Entity is a party to it.

[132] 1.2.4 (2) (a); 1.2.4 (3) (b) (i); 1.2.4 (4) (a) Clearing Rule.

(a) a financial services licensee;

(b) an Australian ADI[133];

(c) an Exempt Foreign Licensee.

To qualify for mandatory clearing, such Financial Entities must pass the quantitative threshold for in-scope products and activities. As a result, only particular large financial institutions may qualify as clearing entities.[134]

3. In-scope products for clearing

The clearing obligation finally applies to defined **Clearing Derivatives[135]** only. These are defined by reference to the underlying and its place of execution. For the threshold calculation[136], additional underlyings may count but the reference to the place of execution remains the same.

a) Eligible underlyings for clearing:

The only products the clearing obligations apply to, are the products defined as Clearing Derivatives in 1.2.3 Clearing Rule. The definition can be summarized as only including interest rate derivatives denominated in Australian Dollars, US Dollars, Euros, British Pounds and Japanese Yen[137]. In no case mandatory clearing is applied to OTC commodity derivatives.

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[133] Authorized Deposit Taking institution according to sec. 9 of the Corporations Act 2001.
[134] There are only ~20 Clearing entities in Australia. They include inter alia Goldman Sachs, JP Morgan, Australia New Zealand Banking Group, UBS and Deutsche Bank. (as published by ASIC https://asic.gov.au/regulatory-resources/markets/otc-derivatives/central-clearing-of-otc-derivatives/clearing-entity-notifications/).
[135] As defined per rule 1.2.3. Clearing Rule and which are those instruments where an actual clearing mandate exists.
[136] See below under 6 c).
[137] Compare ASIC summary at https://asic.gov.au/regulatory-resources/markets/otc-derivatives/central-clearing-of-otc-derivatives/.

b) Exclusion of regulated venues

Furthermore, derivatives traded at a Part 7.2A Market[138], a Regulated Foreign Market or an Exempt Financial Market are excluded from being OTC Derivatives[139] in 1.2.3(7) Clearing Rule:

> *(7) A Derivative is not a Clearing Derivative if:*
>
> *(a) the Derivative is able to be traded (within the meaning of section 761A of the Act) on a Part 7.2A Market, a Regulated Foreign Market or an Exempt Financial Market; and*
>
> *(b) in the case of a Part 7.2A Market, the entry into of the arrangement that is the Derivative:*
>
> > *(i) takes place on the Part 7.2A Market in accordance with the operating rules of the Part 7.2A Market; or*
> >
> > *(ii) is reported to the operator of the Part 7.2A Market in its capacity as operator of the Part 7.2A Market, in accordance with the operating rules of the Part 7.2A Market; and*
>
> *(c) in the case of a Regulated Foreign Market or an Exempt Financial Market, the entry into of the arrangement that is the Derivative takes place on the Regulated Foreign Market or the Exempt Financial Market.*

Regulated Foreign Markets are defined in 1.2.1 Clearing Rule as Designated Contract Markets under the DFA, **Regulated Markets under MiFID II** and other Markets determined

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[138] Part 7.2A Market means a financial market the operator of which is licensed under subsection 795B(1) of the Act, but does not include a financial market operated by an operator specified in regulation 10.15.02 of the Regulations, i.e. ASIC supervised regulated markets.

[139] See rationale: *„We believe that only OTC derivatives should be included in the calculation of the clearing threshold and subject to mandatory central clearing. The focus of the G20 commitments is OTC derivatives, so it is appropriate to limit mandatory central clearing to OTC derivatives. This proposal also recognises that transactions executed on, or reported to the operator of a Pt 7.2A market (or equivalent) are generally subject to existing requirements to clear those derivative transactions.“,* margin 34 in CONSULTATION PAPER CP 231 Mandatory central clearing of OTC interest rate derivative transactions (asic.gov.au).

by ASIC[140]. Exempt Financial Markets are defined in the 1.2.1 Clearing Rule by Reference to the Derivative Transaction Reporting Exemption Instrument[141], they though do not have any practical relevance anymore.

4. In-scope activities

The clearing rules apply to different types of activities:

a) Acting in a representative capacity, which means the entity acting in a capacity as the responsible entity for a registered scheme, or as the trustee of a trust[142].

b) Acting in personal capacity, which means the entity acting in a capacity that is not a Representative Capacity[143].

Both type of activities are in scope of the regulation but subject to separate quantitative thresholds allocated to any of those activity types.

5. Exemptions

Even if in scope from a product perspective, transactions with a *related body corporate*[144] of the Clearing Entity do not have to be cleared (2.1.4 Clearing Rule). As well, Multilateral Portfolio Compression transactions do not have to be cleared (2.1.5. Clearing Rule).

6. Threshold calculation

The threshold is only relevant to Financial Entities as only such are obliged to calculate it and applies on entity level. There is no group aggregation. The main aim of the threshold is to separate system relevant from non-relevant financial market participants[145].

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[140] These other so determined markets can be found in ASIC Regulated Foreign Markets Determination [OTC DET 13/1145] (https://www.legislation.gov.au/Details/F2020C00915) they include inter alia all UK Regulated Markets and numerous markets in Asia.
[141] ASIC Corporations (Derivative Transaction Reporting Exemption) Instrument 2015/844 as in force on 1 October 2020 (https://www.legislation.gov.au/Details/F2020C00930).
[142] 1.2.1. Derivative Transaction Rules.
[143] 1.2.1. Derivative Transaction Rules.
[144] *Exception to Clearing Requirement—Intra-group trades,* 2.1.4 derivatives transaction rules.
[145] CONSULTATION PAPER CP 231 Mandatory central clearing of OTC interest rate derivative transactions (asic.gov.au),see rationale under margin 22-30.

a) Split Threshold

The threshold differentiates between “Financial Entity acting in its Personal Capacity” and “Financial Entity acting in a Representative Capacity” (1.2.7 Clearing Rule). The threshold amount in both capacities is set to AUD 100 billion but **calculated separately** and in full available to any of the two types of activities.

The wording for the Financial Entity acting in its Personal Capacity is as follows:

> *(1) If a Financial Entity holds total gross notional outstanding positions of AUD $100 billion or more in its Personal Capacity on each of two consecutive Calculation Dates, the entity **meets the Clearing Threshold** in its Personal Capacity from the date (**Clearing Start Date**) that is the first Monday after the immediately following Calculation Date.*

b) Reference Period

The reference period is two consecutive Calculation Dates. Calculation Date is defined as each of 31 March, 30 June, 30 September and 31 December in each calendar year (1.2.1 Clearing Rule). As the relevant positions are the gross notional outstanding positions, long running derivatives may be counted into the threshold more than once.

c) Derivative definition for the threshold calculation

According to 1.2.6(1) Clearing Rule, the total gross notional outstanding position to be used for the calculation of the Clearing Threshold includes all derivatives (not limited to clearing derivatives) entered into by **the entity itself** (not on group level) as defined in sec. 761D Corporations Act[146] but excludes regulated venue transactions[147], intra-group transactions and derivatives entered into by Foreign Clearing Entities outside of Australia and not representing Australian schemes or trusts.

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[146] 1.2.1 Clearing Rules defines derivative by a reference to sec. 761D Corporations Act.
[147] Which are Part 7.2A Markets, Regulated Foreign Markets and Exempt Financial Markets.

(*1) A reference in these Rules to the total gross notional outstanding positions held by an entity in a particular capacity is a reference to the entity's total gross notional outstanding positions aggregated across all Derivatives to which the entity is a party in that capacity,* ***but does not include****:*

(a) a position in a Derivative that is not a Clearing Derivative because of subrule 1.2.3(7)[148] *(whether or not it is also not a Clearing Derivative for other reasons); or*

(b) a position in a Derivative entered into with a related body corporate of the entity; or

(c) for an entity:

(i) that is acting in its Personal Capacity and is incorporated or formed outside Australia; or

(ii) that is acting in a Representative Capacity in relation to a scheme or trust that is incorporated or formed outside Australia;

a position in a Derivative:

(iii) that was not booked to the profit or loss account of a branch of the entity located in Australia; and

(iv) that either:

(A) was not entered into in Australia; or

(B) was entered into in Australia before 25 February 2015.

(2) This Rule applies for the purposes of these Rules and paragraph 7.5A.60(2)(a) of the Regulations

d) Exclusion of physically settled derivatives from threshold calculation

Sec. 761D Corporations Act[149] defines derivatives as forward contracts for future settlement beyond a spot period relating to the value of a suitable underlying, including commodities.

[148] Which excludes Regulated Markets, see above.
[149] Sec. 761D subsection 1 Corporations Act.

According to Sec. 761D(3)(a) Corporations Act, however, **physically settled** contracts are excluded from the derivative definition:

> *Subject to subsection (2), the following are **not derivatives** for the purposes of this Chapter even if they are covered by the definition in subsection (1):*
>
> *(a) an arrangement in relation to which subparagraphs (i), (ii) and (iii) are satisfied:*
>
> > *(i) a party has, or may have, an obligation to buy, and another party has, or may have, an obligation to sell, **tangible property** (other than Australian or foreign currency) at a price and on a date in the future; and*
> >
> > *(ii) the arrangement does **not** permit the seller's obligations to be wholly **settled by cash**, or by set-off between the parties, rather than by delivery of the property; and*
> >
> > *(iii) neither usual market practice, nor the rules of a licensed market or a licensed CS facility, permits the seller's obligations to be closed out by the matching up of the arrangement with another arrangement of the same kind under which the seller has offsetting obligations to buy;*
>
> *but only to the extent that the arrangement deals with that purchase and sale;*

e) Exclusion of derivatives traded at a regulated venues.

1.2.6(1)(a) Clearing Rule defines that any derivative traded at a regulated venue in the meaning of 1.2.3(7) Clearing Rule (see above) is not included in the calculation of the Clearing Threshold.

f) Exclusion of intra-group transactions

1.2.6(1)(b) Clearing Rule defines that any derivative entered into with a related body corporate of the entity is not included in the calculation of the Clearing Threshold.

g) Geographical coverage

1.2.6 (1)(c) Clearing Rule stipulates that transactions by non-Australian entities or not representing Australian schemes or trusts and that are

- not booked on an Australian branch of that entity and that are
- entered into outside of Australia

do not count against the Clearing Threshold of such non-Australian entity. A group aggregation is not foreseen anyway as the threshold only applies to the derivatives where the calculating entity itself is a party to.

7. Summary

It has to be concluded that the Australian approach is comparably lenient but still covers and mandates the envisaged group of large international derivative dealers.

For the purpose of this comparison, which focusses on commodity derivative trading of non-financial entities, the most important fact is that neither non-financial market participants nor physical instruments are in scope. The entire system applies to the financial sector only.

Apart from that, the regime is particularly clear and easy to understand. The definition of in-scope entities and in-scope products is not ambiguous and relieves market participants from too complex legal analysis. Further, the thresholds are highest in comparison but – due to the absence of privileged transactions - still easy to handle and able to produce predictable results without giving room to case by case assessments of privileges such as hedging, which as a tendency gives can create legal uncertainty. Finally, Australia applies the approach to strictly limit its regulation to entities and activities which may create risk exposure to the Australian market and neglects a global reach of its regime.

IV. Singapore

1. General

Regulatory oversight over the OTC-derivative market is exercised by the MAS[150] on the basis of the Securities and Futures Act, SFA[151]. This includes the oversight over commodity derivative contracts which were formerly regulated under the Commodity Trading Act, CTA[152]. Nowadays, the CTA governs the remaining spot market segment.

The application of the clearing mandate under the SFA is **particularly lenient**. Not only do the obligations only apply to **licensed banks**, the clearing threshold applies on **entity level**, is comparably high (**"20 bn SGD**) and the entire set of obligations do only extend to **transactions booked in Singapore**.

The relevant legal sources are *part VIB (Clearing of derivative contracts)* of the SFA (**Act**) and the *Securities and Futures (Clearing of Derivatives Contracts Regulations 2018* (**Clearing Regulations**[153]) with further specifications[154].

2. In-scope entities

Generally in scope of the clearing regulation are all "**specified persons**" as defined in Art. 129B Securities and Futures Act[155]

These are:

> (*a) any bank that is licensed under the Banking Act (Cap. 19);*
>
> *(b)any merchant bank approved as a financial institution under the Monetary Authority of Singapore Act (Cap. 186);*

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[150] Monetary Authority of Singapore, see under Monetary Authority of Singapore (mas.gov.sg).
[151] Securities and Futures Act - Singapore Statutes Online (agc.gov.sg).
[152] Commodity Trading Act - Singapore Statutes Online (agc.gov.sg).
[153] Securities and Futures (Clearing of Derivatives Contracts) Regulations 2018 - Singapore Statutes Online (agc.gov.sg).
[154] Which may be read in conjunction with the regulations for mandatory trading of OTC derivatives contracts on organised markets, Securities and Futures (Trading of Derivatives Contracts) Regulations 2019 - Singapore Statutes Online (agc.gov.sg) which contain comparable provisions to the trading mandate under MiFIR and are subject to a similar set of exemptions as the clearing regulations, in particular regarding the threshold.
[155] Securities and Futures Act (Chapter 289) **(SFA)** https://sso.agc.gov.sg/Act/SFA2001#pr129B-.

(c) any finance company licensed under the Finance Companies Act (Cap. 108);

(d) any insurer licensed under the Insurance Act (Cap. 142);

[(e) deleted]

(f) any holder of a capital markets services license; or

(g) any other person who is, or who belongs to a class of persons which is, prescribed by the Authority by regulations made under section 129G for the purposes of this definition.

Out of these categories of specified persons, **all subcategories** (b)-(f) are **explicitly exempt** from the clearing mandate of the act under section 5 of the Regulation[156].

Regarding (a), all licensed banks are as well exempt if their aggregate outstanding notional amount does not exceed the **clearing threshold** of **$20,000,000,000.**

Consequently, the clearing mandate does effectively only apply to licensed banks above the threshold.

Any other market participant apart from banks is out of scope from the beginning and not required to calculate any threshold.

[156] Exemption from section 129C of Act which reads:
5. *The following specified persons are exempt from section 129C of the Act:*
(a) any bank that is licensed under the Banking Act (Cap. 19) whose aggregate outstanding notional amount does not exceed $20,000,000,000.
(i) for the last day of the most recently completed quarter; and
(ii) for last day of each of the 3 consecutive quarters immediately preceding that quarter;
(b) any bank that is licensed under the Banking Act that has been carrying on business for less than one year;
(c) any merchant bank approved as a financial institution under the Monetary Authority of Singapore Act (Cap. 186);
(d) any finance company licensed under the Finance Companies Act (Cap. 108);
(e) any insurer licensed under the Insurance Act (Cap. 142);
(f) any holder of a capital markets services license.

3. In-scope products

Derivative contracts are generally defined in Art. 2 (1) SFA and include physically settled forward contracts where the value depends on the change of a reference value of the underlying[157].

3.1 The clearing mandate as such does only apply to **specified derivative** contracts (Art. 129C SFA). Specified derivatives are defined in the Schedule, par. 1 to the Securities and Futures (Clearing of Derivatives Contracts) Regulations 2018[158].

These are basically only OTC traded fixed for floating interest rate swaps entered into by two specified persons which are non-related entities and the swaps to be booked in Singapore.

3.2 For the **calculation** of the clearing threshold **all derivative** contracts that are not exchange-traded and that are booked in Singapore are relevant (sec. 2 Clearing Regulations).

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[157] Art. 2 (1) SFA, derivatives contract" means
(a) any contract or arrangement under which
(i) a party to the contract or arrangement is required to, or may be required to, discharge all or any of its obligations under the contract or arrangement at some future time; and
(ii) the value of the contract or arrangement is determined (whether directly or indirectly, or whether wholly or in part) by reference to, is derived from, or varies by reference to, either of the following:
(A) the value or amount of one or more underlying things;
(B) fluctuations in the values or amounts of one or more underlying things; or
(b) any contract or arrangement that is, or that belongs to a class of contracts or arrangements that is, prescribed to be a derivatives contract,
but does not include.
(i) securities;
(ii) any unit in a collective investment scheme;
(iii) a spot contract;
(iv) a deposit as defined in section 4B of the Banking Act (Cap. 19), where the deposit is accepted by a bank licensed under that Act or a merchant bank approved as a financial institution under the Monetary Authority of Singapore Act (Cap. 186);
(v) a deposit as defined in section 2 of the Finance Companies Act (Cap. 108), where the deposit is accepted by a finance company as defined in that section of that Act;
(vi) any contract of insurance in relation to any class of insurance business specified in section 2(1) of the Insurance Act (Cap. 142); or
(vii) any contract or arrangement that is, or that belongs to a class of contracts or arrangements that is, prescribed not to be a derivatives contract.

[158] Securities and Futures (Clearing of Derivatives Contracts) Regulations 2018 (**Clearing Regulations**) https://sso.agc.gov.sg/SL/SFA2001-S264-2018?DocDate=20191010&ValidDate=20191011&Timeline=On.

a) **Exchange traded derivatives** are defined in Art. 2 (1) SFA and refer to any kind of derivative contract which is standardized, executed on an organized market and cleared or settled by a clearing facility[159].

Organized markets are further defined on a qualitative basis and include

> *a place at which, or a facility (whether electronic or otherwise) by means of which, offers or invitations to exchange, sell or purchase derivatives contracts, securities or units in collective investment schemes, are regularly made on a centralised basis, being offers or invitations that are intended or may reasonably be expected to result, whether directly or indirectly, in the acceptance or making, respectively, of offers to exchange, sell or purchase derivatives contracts, securities or units in collective investment schemes (whether through that place or facility or otherwise)*[160]

irrespective of any formal recognition.

b) **Booked in Singapore** in defined is sec. 2 Clearing Regulations and in relation to a derivatives contract, means the entry of the derivatives contract on the balance-sheet or the profit and loss accounts of a person where

> *(a) the person is a party to the derivatives contract;*
>
> *(b) the person's place of business is in Singapore; and*
>
> *(c) the balance-sheet or the profit and loss accounts relate to the person's business in Singapore.*

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[159] "exchange-traded derivatives contract" means a derivatives contract:
(a) that is executed on an organised market and is or will be cleared or settled by a clearing facility under an arrangement, process, mechanism or service by which the parties to the derivatives contract substitute or will substitute, through novation or otherwise, the credit of the clearing facility for the credit of the parties to the derivatives contract; and
(b) the contractual terms (other than price) of which
(i) are in the same form as the contractual terms of other derivatives contracts of the same type that are executed on the organised market on which the derivatives contract is executed; and
(ii) conform to a standard that is provided under the business rules or practices of the organised market on which the derivatives contract is executed.

[160] First Schedule Part I SFA, sec. 1 definition of organised market.

Consequently, the regulation and the clearing mandate does **not include** transactions of affiliates based **outside Singapore** without any Singaporean nexus as per (a)-(c) above.

Transactions of such Singaporean entities executed on organized markets in or outside of Singapore are further not considered due to the limitation to OTC-derivatives and the exclusion of exchange traded derivatives in the first place.

The determination of the in-scope products therefore follows a particularly narrow approach.

- Third country business not booked in Singapore is not considered
- Transactions executed and cleared at organized markets are out of scope from the beginning
- Business of affiliates is not considered in determining the individual notional amount for the threshold assessment.

4. Exemptions

See above under 2, exemptions apply on the level of **in-scope entities**. Additional exemptions regarding the purpose of activities such as hedging or the nature of the instrument are not foreseen.

5. Threshold calculation

The clearing threshold for the in-scope entities amounts to **20 bn SGD** aggregate outstanding notional amount (sec. 5 (a) Clearing Regulations).

The calculation has to be done

(i) for the last day of the most recently completed quarter; and

(ii) (ii) for last day of each of the 3 consecutive quarters immediately preceding that quarter (sec. 5 (a) Clearing Regulations).

The aggregate outstanding notional amount is defined in sec. 2 Clearing Regulations (with the derivative contracts as defined under 3. above) as

> *the aggregate of the notional amounts of every derivatives contract:*
>
> *(a) which is not an exchange-traded derivatives contract;*
>
> *(b) to which the bank is a party;*
>
> *(c) which is booked in Singapore; and*
>
> *(d) which is outstanding.*

Other instruments are not considered and group aggregation does not apply.

If the bank exceeds the threshold with its outstanding notional amount on all four ends of a quarter, it is in scope of the clearing mandate.

6. Summary

In comparison, the Singaporean approach appears to be **most beneficial** for non-financial entities, which are out of scope in the first place. The entire system applies to licensed banks only.

All further limitations in scope and geographical coverage bring further relief to the in-scope banks. These limitations are

- a comparably **high clearing threshold** per entity **absent** any **group aggregation**;
- the **exclusion of** cleared **venue traded** derivatives including third country venues;
- the limited geographical coverage due to the application to transactions **booked in Singapore** only.

Therefore, the Singaporean approach leaves maximum headroom for energy commodity transactions of non-financial market participants and is to a large extent comparable to the Australian approach.

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