European Market Infrastructure Regulation

WesternUnion WU | Business Solutions

EU rules affecting trading in derivatives are now in force under the EMIR regime. This pamphlet summarises certain of the obligations that apply to counterparties transacting derivatives who are subject to EMIR and sets out key points for consideration by customers of Western Union International Bank GmbH ("WUIB") in order to facilitate implementation of the EMIR regime.[1]

Background

What is the background to EMIR?

In September 2009, the G20 countries made an international commitment to address risks related to the over the counter (OTC) derivatives market. As a result, 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 (commonly known as the "European Market Infrastructure Regulation" or "EMIR") came into force on 16 August 2012. The EMIR requirements were introduced in phases.

What does EMIR require?

The main requirements of EMIR applicable to participants in the derivatives market are:

- Risk Mitigation: "risk mitigation" rules applying to non-centrally cleared OTC derivative contracts, including timely confirmation, portfolio reconciliation, dispute resolution and mandatory margining requirements;
- Reporting: reporting OTC derivative contracts to trade repositories;
- Recordkeeping: certain records need to be maintained in relation to OTC derivative contracts; and
- Clearing: certain OTC derivative contracts must be cleared with an authorised or recognised central counterparty ("CCP").

Further information on each of these requirements is set out below.

Who does EMIR apply to?

The application of EMIR is not limited to regulated entities. In essence, EMIR applies to any entity established in the EU which has entered into a derivatives contract. In some circumstances it also applies to entities established outside the EU. It applies to WUIB and we believe that it applies to clients that enter into OTC derivative contracts with WUIB.

What products does EMIR apply to?

EMIR applies to derivative contracts (including forward and options currency transactions). Transactions such as these may be concluded under WUIB's standard terms and conditions. Note that spot foreign exchange transactions are not subject to EMIR.

1 The EMIR pamphlet is provided for information only and does not constitute legal advice. It provides a simplified overview of the application of EMIR and does not discuss the detail of any of the obligations that apply under EMIR. Western Union International Bank GmbH does not accept any liability to any person for the information which is provided in this document. More information on the matters referred to in this document can be found at the European Securities and Markets Authority's site; see http://www.esma.europa.eu/page/post-trading. We strongly recommend that you seek legal advice in order to fully understand the impact that EMIR will have on your business.

Counterparty classifications under EMIR

What are the different categories of counterparty for the purposes of EMIR?

There are two main categories of counterparty for the purposes of EMIR, namely, financial counterparties and non-financial counterparties.

Financial Counterparties ("FCs"): FCs include credit institutions, investment firms and insurance/reinsurance undertakings. WUIB is an FC.

Non-Financial Counterparties ("NFCs"): NFCs are undertakings which are established in the EU and which are not classified as FCs. There are two categories of NFCs, namely, NFCs whose average trading levels in OTC derivative contracts over a certain period of time put them above the EMIR clearing threshold (**"NFC+s"**), and NFCs whose levels of trading in OTC derivative contracts are low enough to fall below the clearing threshold (**"NFC-s"**). (See below for further detail).

What is the difference between a NFC+ and a NFC-?

An NFC+ is an NFC whose positions in OTC derivative contracts (excluding all hedging positions permitted to be excluded by EMIR) exceed the clearing threshold for a period of time, as specified below.

An NFC- is any other NFC.

The clearing threshold varies according to the class of OTC derivative contract and is calculated based on the total gross notional amounts of OTC derivative contracts entered into by an NFC, as set out in the table below. Where an NFC exceeds one of these thresholds on any given day, it must immediately notify the European Securities and Markets Authority ("ESMA") and its national competent authority. Where an NFC exceeds any of these thresholds, on a rolling average basis, over a 30 working day period, such NFC becomes an NFC+ and enhanced obligations will apply to it under EMIR.

The threshold is assessed on a group-wide basis of all non-financial entities within the NFC's worldwide group and not by reference to individual entities. Therefore, NFCs must calculate the total gross notional amount of OTC derivative contracts entered into by each entity in their group (as long as those entities are also NFCs, or would be classed as NFCs were they established in the EU). It is this total amount of gross notional across the NFC's group (excluding all hedging positions permitted to be excluded by EMIR) that will determine whether the NFC falls above or below the clearing threshold.

Relevant Class of OTC Contract	Clearing Threshold (Gross Notional Amount)
Credit Derivative Contracts	EUR 1 billion
Equity Derivative Contracts	EUR 1 billion
Interest Rate Derivative Contracts	EUR 3 billion
Foreign Exchange Derivative Contracts	EUR 3 billion
Commodity Derivative Contracts and Others	EUR 3 billion

The calculation of the clearing threshold is complicated and should be considered carefully. Legal advice should be obtained if you are uncertain of your status under EMIR.

Why is the difference between an NFC+and an NFC- important?

It is important that you are correctly classified under EMIR as this classification determines the application and extent of the requirements of EMIR. For example, certain requirements apply to NFC+s only, such as the obligation to clear OTC derivative contracts declared subject to the clearing obligation, the requirement to mark transactions to market or model on a daily basis and the requirement to collect a mandatory amount of collateral in respect of uncleared OTC derivative contracts. In addition, the timely confirmation deadlines are shorter and portfolio reconciliation requirements are more frequent for NFC+s.

Obligations under EMIR[2]

What is the record keeping obligation?

All NFCs are required to keep records of any derivative contract they have concluded as well as any modification to any such derivative contract (whether OTC or exchange traded) for 5 years following the termination of the derivative contract.

What is the transaction reporting obligation?

All NFCs must report the details of any derivative contract (whether OTC or exchange traded) to a registered or recognised trade repository no later than the working day following the conclusion, modification or termination of the derivative contract. Although reporting may be undertaken by one of the counterparties to the transaction (or by a third party appointed for this purpose), it is important to bear in mind that reporting will remain the legal obligation of both counterparties to the transaction, whether they have delegated it to another party or not.

This obligation came into force on 12 February 2014. WUIB has included terms in its standard terms and conditions relating to derivative contracts pursuant to which WUIB will report the derivative contracts which you enter into with WUIB to a trade repository on your behalf.

2 This is not a comprehensive overview of the requirements which will apply to you under EMIR, for example, it does not cover the marking-to-market/-model requirement or the portfolio compression requirement to which you may be subject. You should consult your legal advisers for a full analysis of how EMIR will affect you.

What are the risk mitigation rules for uncleared OTC derivative contracts?

The risk mitigation rules applying to counterparties which have entered or are entering into uncleared OTC derivative contracts are as follows:

- Timely Confirmation Requirements
- Portfolio Reconciliation
- Dispute Resolution
- Mandatory Margining

Timely Confirmation Requirements

FCs and NFCs must confirm uncleared OTC derivative contracts by set deadlines. Note that "confirmation" in this context means the documentation of the agreement of the counterparties to all the terms of an OTC derivative contract. The "confirmations" which we would ordinarily send to you in writing or by email in order to evidence the terms of the relevant OTC derivative contract, along with WUIB's terms and conditions, should be sufficient for these purposes. The relevant deadlines are set out below.

Timely Confirmation Deadlines	Credit default swaps and interest rate swaps	Equity swaps, foreign exchange swaps, commodity swaps and all other uncleared OTC derivative contracts
FCs and NFC+s	T+1	T+2 until 31 August 2014 and T+1 thereafter
NFC-s	T+3 until 31 August 2014 and T+2 thereafter	T+4 until 31 August 2014 and T+2 thereafter

Where "T" represents the date of entering into the OTC derivative contract

In order to comply with the short timely confirmation deadlines of EMIR, WUIB has introduced specific terms governing the way in which OTC derivative contracts between you and WUIB will be confirmed. Please, therefore, ensure that you have procedures and arrangements in place to check confirmations sent to you by WUIB as soon as possible.

WUIB, as an FC, must have procedures in place to report OTC derivative contracts which are not confirmed within the deadlines set out above to its national competent authority.

Portfolio Reconciliation

EMIR requires FCs and NFCs, such as yourselves, to agree arrangements with regard to portfolio reconciliation before trading uncleared OTC derivatives contracts. Portfolio reconciliation enables counterparties to review the portfolio of trades between them to ensure their books and records are aligned and the details of each trade are accurately recorded. The intention is to identify any discrepancies in the material terms of the OTC derivatives contracts at an early stage.

Portfolio reconciliation should cover key trade terms and the valuation attributed to the relevant OTC derivative contracts. The frequency of the portfolio reconciliation exercise varies depending on the size of your portfolio and classification under EMIR. For example, for NFC-s with 100 or fewer OTC derivative contracts outstanding with WUIB, portfolio reconciliation need only be carried out once a year.

The portfolio reconciliation obligation entered into force on 15 September 2013 and, accordingly, WUIB has introduced supplementary terms which set out the terms of reconciliation which will apply between WUIB and its customers.Any discrepancies identified through the reconciliation process may result in a dispute resolution procedure being triggered (see below).

Dispute Resolution

EMIR requires FCs and NFCs transacting uncleared OTC derivative contracts to agree procedures for the identification, recording, monitoring and resolution of disputes relating to OTC derivative contracts (including disputes arising from the reconciliation procedure, as noted above).

The dispute resolution obligation entered into force on 15 September 2013 and, accordingly, WUIB has introduced specific terms which set out the dispute resolution procedures which will apply between WUIB and its customers.

WUIB, as an FC, must report certain unresolved disputes to its national competent authority.

Mandatory Margining

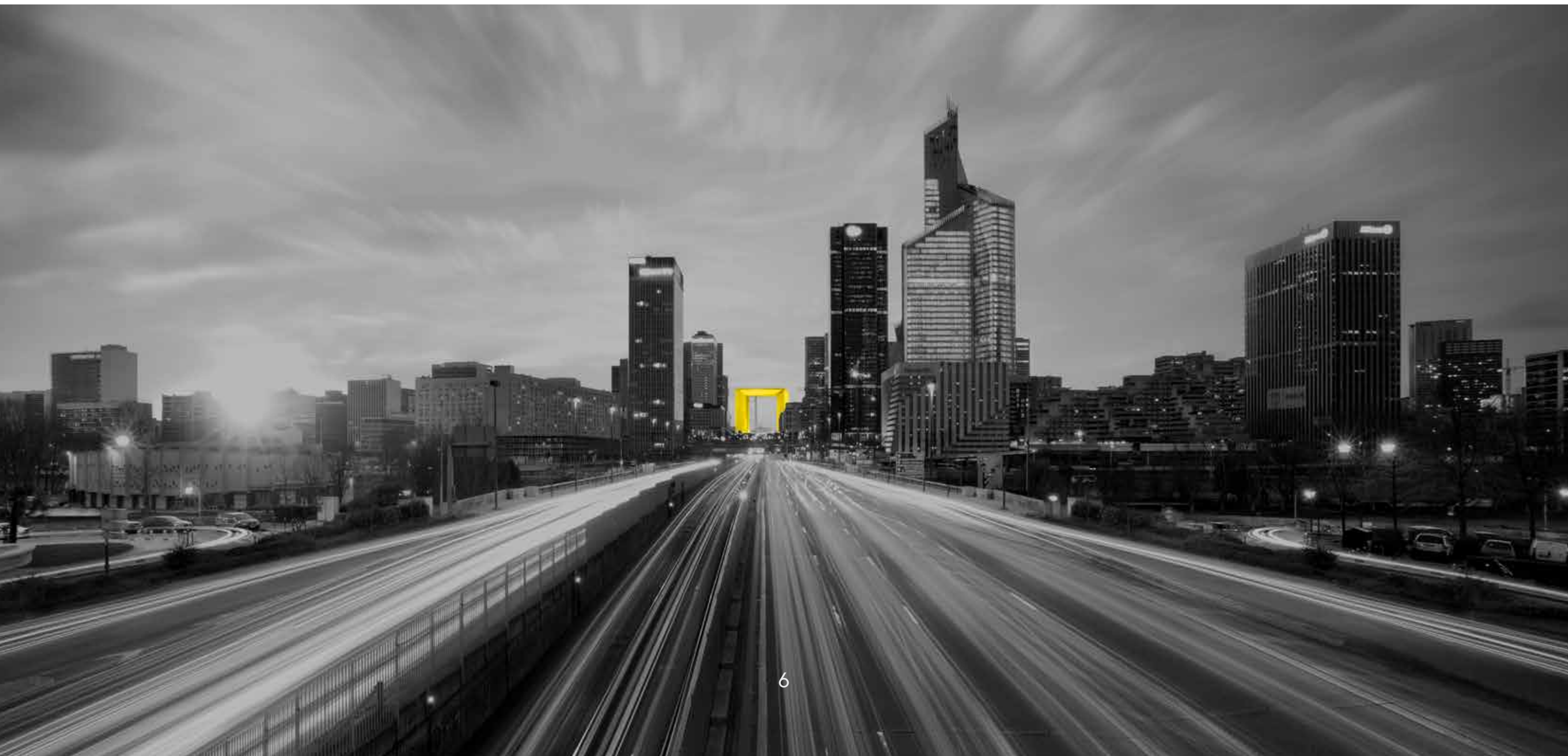
Certain OTC derivative contracts are subject to the mandatory margining obligation under EMIR if they are not cleared through a CCP. In the event that OTC derivative contracts entered into between you and WUIB are affected by this requirement, we will contact you in relation to WUIB's policies in this regard.

What is the clearing obligation?

Certain OTC derivative contracts may in future become subject to a "clearing obligation" under EMIR if they are declared subject to clearing by the EU Commission.

We do not anticipate that the derivatives which you transact with WUIB will be amongst the classes of derivatives declared subject to mandatory clearing at this time.

If and when a clearing obligation is (or appears likely to be) declared with respect to the OTC derivative contracts traded between you and WUIB, WUIB expects to contact you to explain the process for determining whether such contracts will need to be cleared. This requirement will not affect customers which are NFC-s.



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