

**MEMO# 27980**

March 25, 2014

# **EU Commission Responds to Request by EU Regulators for Clarification Regarding Classification of Certain Financial Instruments as Derivatives**

[27980]

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TO: DERIVATIVES MARKETS ADVISORY COMMITTEE No. 20-14

ICI GLOBAL MEMBERS No. 11-14

INVESTMENT ADVISER MEMBERS No. 10-14

INTERNATIONAL MEMBERS No. 10-14 RE: EU COMMISSION RESPONDS TO REQUEST BY EU REGULATORS FOR CLARIFICATION REGARDING CLASSIFICATION OF CERTAIN FINANCIAL INSTRUMENTS AS DERIVATIVES

The EU Commission has sent a letter in response to the request by the European Securities and Markets Authority (“ESMA”) for clarification regarding whether the definition of “derivatives” for purposes of the European Market Infrastructure Regulation (“EMIR”) would cover certain foreign exchange (“FX”) forwards and physically settled commodity forwards. [\[1\]](#) In its request, ESMA noted that EU Member States have not adopted a single or common definition of “derivatives,” which could result in inconsistent application of EMIR. Specifically, ESMA requested that the EU Commission clarify the following: (1) the definition of currency derivatives in relation to (a) the frontier between spot and forward and (b) their conclusion for commercial purposes; and (2) the definition of commodity forwards that can be physically settled.

With respect to FX forwards, the letter states that the EU Commission’s Internal Market and Services Directorate General (DG MARKT) will be assessing options for action to ensure consistent application of EMIR. The letter seeks assistance from ESMA on how the definition of FX forward has been transposed into national law by the Member States. The EU Commission also asks for information on the commonly accepted delivery period for currencies in the Member States and the developments in the foreign exchange markets since the implementation of Markets in Financial Instruments Directive (“MiFID”). The Commission also notes that the notion of “commercial purpose” is only foreseen as a criterion for physically settled commodity derivative contracts.

With respect to the definition of commodity forwards that can be physically settled, the EU

Commission states that this issue was discussed during the MiFID II negotiations. The Commission believes that it would not be appropriate to develop level 2 proposals under the current MiFID, which would prejudice the regulatory work under MiFID II. The Commission invites ESMA to assess the status of physically settled commodity forwards in preparation for its advice to the Commission under MiFID II.

Jennifer S. Choi  
Senior Associate Counsel Securities Regulation

#### **endnotes**

[1] Letter from Jonathan Faull, Director General for Internal Market and Services, European Commission, to Steven Maijor, Chair ESMA, dated February 26, 2014 available at [http://www.esma.europa.eu/system/files/ares2014513399\\_ec\\_response\\_on\\_classification\\_of\\_financial\\_instruments.pdf](http://www.esma.europa.eu/system/files/ares2014513399_ec_response_on_classification_of_financial_instruments.pdf); see letter from Steven Maijor, Chair, ESMA, to Michael Barnier, Commissioner for Internal Market and Services, European Commission, dated February 14, 2014, available at [http://www.esma.europa.eu/system/files/2014-184\\_letter\\_to\\_commissioner\\_barnier\\_-\\_classification\\_of\\_financial\\_instruments.pdf](http://www.esma.europa.eu/system/files/2014-184_letter_to_commissioner_barnier_-_classification_of_financial_instruments.pdf). For a summary of ESMA's request, see ICI Memorandum No. 27895 (Feb. 18, 2014), available at [http://www.ici.org/my\\_ici/memorandum/memo27895](http://www.ici.org/my_ici/memorandum/memo27895).

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