



EUROPEAN CENTRAL BANK

EUROSYSTEM

5.11.2013

**Françoise Jaulin**  
Deputy Head of Division  
Financial Operations Services

# OTC derivatives in the EU and the US: latest regulatory developments

Operational Managers Contact Group

DISCLAIMER: the views expressed in this presentation are solely those of the author and do not necessarily represent the views of the ECB

# What changed in regulation in the FX market since the last OMCG meeting?

- 1 The European Market Infrastructure Regulation (EMIR)
- 2 New requirements entered into force since the last OMCG
- 3 Timeline evolution for remaining implementation
- 4 Third country regulatory equivalence under EMIR – DFA

# the European Market Infrastructure Regulation (EMIR)

entered into force on 16 August 2012

With the **objectives**:

- to create a new regulatory framework for counterparties to derivative contracts, central counterparties (CCPs), and trade repositories
- to manage counterparty credit risk more effectively
- to increase transparency and stability of OTC derivative markets

**Instruments concerned:** options, swaps, forwards and foreign exchange derivatives are covered within MiFID (Markets in Financial Instruments Directive) while commodity derivatives and foreign exchange spot trades are not derivatives under the relevant provisions of MiFID.

**Reminder:**

EMIR is imposing obligations on centrally clearing OTC derivatives (through CCP), on implementing risk mitigation techniques for uncleared OTC trades, and reporting on all derivatives contract to TR

MiFIR/MiFID is dealing with imposing pre-trade transparency requirements associated with trading venues in respect of bonds, structured finance products, emission allowances and derivative

EMIR is **applicable** to financial counterparties and non-financial counterparties (threshold) undertaking some activities in derivatives in EEA or outside

# New requirements entered into force since last OMCG:

## **Risk Mitigation for non centrally cleared OTC derivative contracts**

On 15 September 2013 following **new risk mitigation measures** for non centrally cleared OTC derivatives went into force for all types of counterparties :

1. Portfolio Reconciliation
2. Portfolio Compression
3. Dispute Resolution

All Central Banks of the EU are exempted from these requirements i.e they do not apply to the ESCB nor to its counterparties when trading with the ESCB.

## **Initial and variation margins** for non-centrally cleared FX swaps and forwards

**On 02.09. the BCBS/IOSCO announced that the new framework** exempts *physically settled* FX forwards and swaps from *initial margin* requirements (only variation margin on these derivatives should be exchanged in accordance with Basel Committee supervisory guidance and standards)

Phase in foreseen for VM requirements is 01/12/2015.

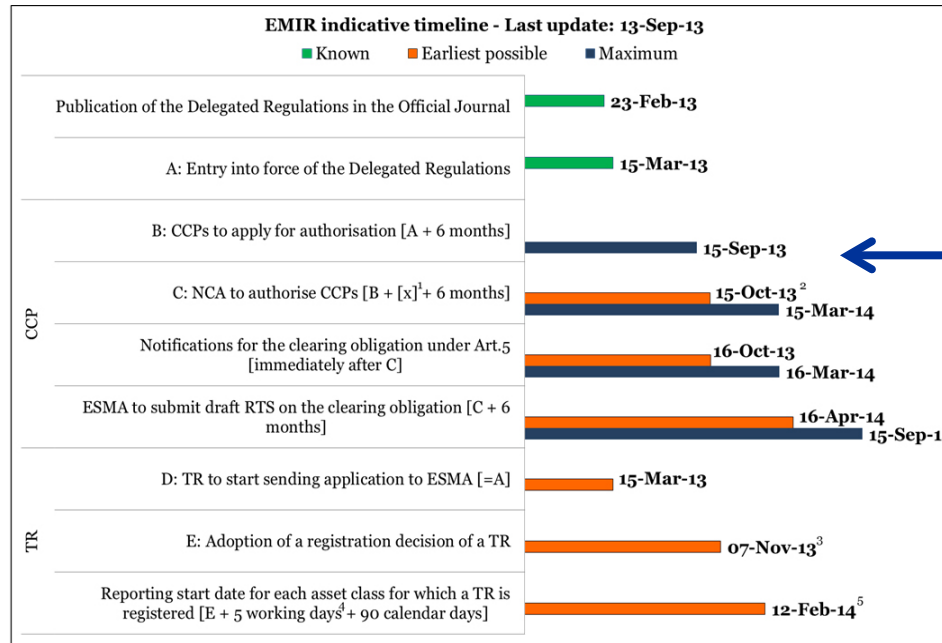
# New requirements entered into force since last OMCG:

## Initial and variation margins for non-centrally cleared FX swaps and forwards

Concretely after issuance of BCBS/IOSCO final policy framework, national EU and US supervisors must now consider to implement the framework (timing not yet clear); **open issues** i.a.:

- **Definition of “financial firms” and “systematically important non financial entities”**
- **Definition of eligible collateral** i.e. could include cash, high quality government securities, high quality corporate bonds, high quality covered bonds, equities included in major stock indices and gold
- Regulation **of inter affiliate transactions**
- Re **hypothecation of margin** (allowed for VM without any threshold, subject to very strict conditions for IM)

# Timeline evolution for remaining implementation



Request for equivalence

- (1) [x] is the time needed for the determination of the completeness of the application sent by CCP to NCA.
- (2) On the basis of the information available so far, ESMA's best estimate is that the first CCP authorisation is not likely to take place before 15 October 2013. This should not be understood as meaning that any authorisation will necessarily be granted on 15 October 2013.
- (3) On the basis of the information available so far, ESMA's best estimate is that the adoption of the registration decision of the first TR(s) is not likely to take place before 7 November 2013. This should not be understood as meaning that the registration decision will necessarily be adopted on 7 November 2013. The exact date on which the registration decision is adopted will depend on the completeness of the TR's application and its compliance with the EMIR provisions.
- (4) The registration decision takes effect on the fifth working day following its adoption.
- (5) The reporting start date depends on the actual date of the registration of the first TR(s).

Source: ESMA

ESMA has published a report on equivalence assessment and submitted to the EC. Feedback not expected before June 2014

As regards TR, ESMA expects to make first registration decision for Trade Repositories on 7 November 2013  
Consequently, counterparties' reporting to trade repositories is not expected to start before February 2014

# Available list of CCPs having applied for recognition under EMIR

Non-EU central counterparties (CCPs) providing clearing services directly to EU clearing members must apply for recognition under EMIR by 15 September 2013.

From info received by ESMA so far and publicly available the following indicative list of CCPs that have applied for recognition, have been compiled (not exhaustive or definitive):

1. Asigna – the Mexican CCP for all derivatives transactions on MexDer;
2. ASX Clear (Futures) Pty – the Australian CCP for exchange-traded and over-the-counter (OTC) derivatives;
3. Brazilian CCPs within the BVMF Group: 1) CBLC Clearinghouse, 2) Derivatives Clearinghouse, 3) Securities Clearinghouse, and 4) Foreign Exchange Clearinghouse;
4. Central Depository Pte Limited (CDP) – the cash market CCP in Singapore;
5. CME Clearing – the U.S. CCP for derivatives traded on several venues within the CME Group as well as some OTC derivatives;
6. Contrapartos Central de Valores (CCV) – the cash market CCP in Mexico;
7. Dubai Commodities Clearing Corporation (DCCC) – the CCP for Dubai Gold and Commodities Exchange;
8. ICE Clear Credit – the U.S. CCP clearing credit default swaps (CDS);
9. ICE Clear U.S. – the CCP serving the agricultural, currency, equity index, natural gas and power markets of ICE Futures U.S.;
10. Japan Securities Clearing Corporation – the Japanese CCP for cash products as well as exchange-traded and OTC derivatives;
11. Korea Exchange – the in-house CCP operated by the stock exchange in South Korea, clearing cash products as well as exchange-traded derivatives;
12. Options Clearing Corporation (OCC) – the U.S. CCP for exchange-traded derivatives;
13. Oslo Clearing – the Norwegian CCP for equities, financial derivatives and securities lending products;
14. SAFCOM – the South African CCP for cash markets and exchange-traded derivatives;
15. SGX-DC – the Singaporean CCP for exchange-traded and OTC derivatives;
16. SIX x-clear – the Swiss CCP for cash markets.

For CCPs with clearing members that are branches of European institutions, a complete application submitted by 15 September 2013 will allow these members to continue their current market operations during the review period set to last until mid-June 2014, according to the current timetable.

If the CCP does not apply, these members will have to cease clearing via that CCP from mid-September onwards.



# Third country regulatory equivalence under EMIR – DFA

On 1 September ESMA issued an advice to the EC in respect of the equivalence between the US regulatory regime and the EU regulatory regime under EMIR in respect of:

- 1. the recognition of third country CCPs,**
- 2. the recognition of Trade Repositories (TRs)**
- 3. the clearing obligation, reporting obligation, non-financial counterparties and risk mitigation techniques for uncleared trades**

No public consultation on this report but just factual comparison of the rules between EU and foreign jurisdictions on how to incorporate differences





# Third country regulatory equivalence under EMIR – DFA

## 1. Conclusion on CCPs

“**CCPs authorised in the US do comply with legally binding requirements** which are equivalent to the requirements laid down in Title IV (Requirements for CCP’s) **of EMIR.**”

Nonetheless, ESMA would **only grant recognition to CCPs** authorised in the US:

- **which have in fact adopted internal policies, procedures, rules, models and methodologies**
- **which incorporate provisions that are broadly equivalent to the legally binding requirements for CCPs under EMIR**

If a CCP authorised in US and recognised by ESMA and subsequently makes changes to its internal rules,....., then that CCP could no longer qualify for recognition (Art. 25(5) EMIR)

# Third country regulatory equivalence under EMIR – DFA

## 2. Conclusion on trade repositories

ESMA considers that TRs authorised in the US do comply with legally binding requirements which are equivalent to the requirements laid down in EMIR, where such TRs have adopted internal policies, procedures, rules, models and methodologies that constitute legally binding requirements and where they incorporate provisions which are broadly equivalent to the legally binding requirements for TRs under EMIR in the following areas:

- **Operational separation of ancillary services**
- **Collection of data**
- **Valuation and collateral**

Current status is:

- **Most of SEC rules** related to TRs are **not yet final**
- **Differences as regards data to be reported** on e.g.
  - scope of data to be reported
  - valuation and collateralisation of exposures
- **Differences on restrictions of access**
- **Differences also in the segregation of ancillary services** that could impact on the safety and stability of TRs in their business conduct

**ESMA considers the US legal, supervisory and enforcement arrangements broadly equivalent** to the requirements laid down in Article 9 of EMIR (**Reporting obligation**) for the purpose of Article 13 of EMIR (**Mechanism to avoid duplicative or conflicting rules**).i.e. **reciprocity is not completely fulfilled**

ESMA considers the effective supervision and enforcement of trade repositories and the **guarantees of professional secrecy equivalent to the EU regime**.i.e. **ESMA is reciprocal to CFTC**

# Third country regulatory equivalence under EMIR – DFA

## 3. Conclusion on mechanism to avoid potential duplicative or conflicting requirements

With respect to the **implementing act on equivalence to be adopted by the Commission** under Article 13(2) of EMIR (equivalence of legal, supervisory and enforcement arrangements of a third country) for the US regime, **ESMA advises the Commission for recognised equivalence regime for:**

- Clearing obligation
- Timely confirmation
- Portfolio reconciliation
- Portfolio compression

BUT

**Dispute resolution** is not equivalent to that of EMIR

**Bilateral margins** and capital cannot be assessed and a decision on equivalence should be postponed;

**Effective supervisory and enforcement arrangements** includes legally binding requirements that are broadly equivalent to those of EMIR (see previous slide).

Hence the “**conditional equivalence**” concept introduced by ESMA

Suggest a willingness to compromise from ESMA instead of refusing equivalence

BUT introduce **confusion**, lots of possible scenarios....