

OTC Clearing in Europe

By Will Acworth and Joanne Morrison

ESMA Proposes Schedule for Central Clearing of Interest Rate and Credit Default Swaps

The European Securities and Markets Authority on July 11 launched its first round of consultations to determine which classes of swaps will be subject to mandatory central clearing. The two consultation papers seek stakeholders' views of draft regulatory standards for the clearing of interest rate swaps and credit default swaps and both propose a phased-in approach to mandated central clearing.

Under the proposed schedule, the first category of participants subject to the clearing mandate would include firms that already clear interest rate swaps or CDS at an approved clearinghouse such as Nasdaq OMX, Eurex and LCH.Clearnet. This group would be required to clear trades six months after ESMA publishes its final rules. ESMA determined this group would include 102 different entities.

The second group, which includes all other financial institutions such as buy-side companies and alternative investment firms, would be required to start clearing 18 months after the rules are published.

The final group, which includes smaller buy-side firms, would be required to comply with the clearing mandate some time in 2016.

For IRS, the clearing mandate would cover basis swaps, fixed-to-floating swaps, forward rate agreements and overnight index swaps on a range of currencies and maturities. For CDS, the four indices covered are iTraxx Europe Main, iTraxx Europe Crossover, iTraxx Europe High Volatility and iTraxx Europe Senior Financials.

ESMA Clarifies Clearing Obligations for Non-EU Clearing Firms

On July 10, the European Securities and Markets Authority issued an updated "Questions and Answers" on the European Market Infrastructure Regulation. The Q&A includes a new section clarifying that non-EU members of European clearinghouses are subject to the segregation requirements in EMIR.

Under these requirements, clearing firms must offer their clients the choice between omnibus client segregation and individual client segregation and inform them of the costs and level of protection associated with each option.

"The references to clearing members in Article 39 are not limited to EU clearing members, so all clearing members of EU CCPs are required to comply," the Q&A states. "Similarly, the references to clients in Article 39 are not limited to EU clients. CCPs are expected to require all clearing members to comply with the relevant EMIR provisions through their rules."

In case of a conflict between these requirements and a third country insolvency regime, the Q&A states that clearing firms should offer "alternative possibilities" such as clearing solutions provided by an affiliate or other clearing members, or alternatively disclose the risks of using a non-EU clearing member "in full to the client at the outset of the relationship."

The Q&A also clarifies that non-EU pension funds are not eligible for the clearing exemption provided under EMIR to EU pension funds.

EU to Grant CCP Equivalence for Five Asian Nations

On June 27, Michel Barnier, European Commissioner for Internal Market and Services, announced that he will propose that the European Commission adopt "equivalence" decisions to allow clearinghouses from five countries outside of the EU to clear EU transactions. The countries are Japan, Singapore, Australia, Hong Kong and India.

Barnier added that the EU will be able to adopt equivalence decisions for the U.S. if the CFTC also gives "effective equivalence" to third country CCPs. "If the CFTC also gives effective equivalence to third country CCPs, deferring to strong and rigorous rules in jurisdictions such as the EU, we will be able to adopt equivalence decisions very soon," Barnier said. "I look forward to continuing my discussions with U.S. partners as a priority matter."

IOSCO Opens Information Repository for Clearing Requirements

The International Organization of Securities Commissions on Aug. 5 unveiled an information repository for clearing requirements for OTC derivatives. The repository provides regulators and market participants with consolidated information on the clearing require-

Nine Clearinghouses Pass ESMA Hurdle

The European Securities and Markets Authority on Aug. 4 updated its list of recognized central counterparties to include CME Clearing Europe. The authorization covers all OTC derivatives and futures currently cleared by CME Clearing Europe, including interest rate swaps, energy swaps and foreign exchange futures.

This recognition enables CME Clearing Europe to offer clearing services and activities in the European Union. As of August, there were nine derivatives that have received such recognition from ESMA.

KEY:

- OTC
- Exchange-Traded
- ▲ Both OTC and Exchange-Traded

ESMA-Authorized CCPs (as of August 2014)

CCP	Country of Establishment	Asset Classes of Derivatives Cleared							
		Equity	Debt	Interest Rates	Credit	Foreign Exchange	Commodity	Emission	Freight
Cassa di Compensazione e Garanzia S.p.A.	Italy	●					●		
CME Clearing Europe Ltd.	United Kingdom			■		●	▲		■
Eurex Clearing AG	Germany	●	▲	▲		●	●	●	
European Commodity Clearing	Germany						▲	▲	▲
KDPW_CCP	Poland	●	●	▲		●			
Keler CCP	Hungary	●	●	●		●	●		
LCH.Clearnet Ltd.	United Kingdom	▲	■	■		■	▲	■	▲
LCH.Clearnet S.A.	France	●			■	●	●		
Nasdaq OMX Clearing AB	Sweden	▲	▲	▲			▲	▲	●

Source: ESMA

ments of different jurisdictions. It sets out clearing requirements on a product-by-product level and any exemptions from them. The information in the repository will be updated quarterly. IOSCO established the repository in February and until now it has been available only to IOSCO members.

Hedge Fund Group Issues OTC Clearing Guidelines

The Alternative Investment Management Association, a London-based association of hedge funds, published a “guide to sound practices for OTC derivatives clearing” on July 1. The guidelines, which are available only to AIMA members, provide information on the regulatory framework in the U.S. and European Union. AIMA also published a questionnaire to help asset managers conduct due diligence on clearing firms and clearinghouses.

Eurex Issues White Paper on Benefits of Clearing

Eurex issued a 37-page paper describing how central clearing reduces systemic risks in three main ways: reducing interconnectedness, protecting market participants from clearing member defaults, and providing independent risk management.

The paper also addressed the need for “strenuous CCP governance and prudent risk standards” given that clearinghouses concentrate risk. The paper analyzes how to ensure the resilience of the clearinghouses themselves and the stability of the overall market structure, and outlines several principles for clearinghouse recovery and resolution planning. ■■

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