



Brussels, 13 May 2013

Practical implementation of the EMIR framework to non-EU central counterparties (CCPs)

Regulation No 648/ 2012 of 4 July 2012 on OTC derivatives, central counterparties and trade repositories ('EMIR') introduces a new recognition procedure for central counterparties (CCPs) that are established outside the European Union (EU) but wish to provide services to market participants that are established in the Union. The purpose of this memo is to specify how this recognition procedure will be implemented.

What CCPs are subject to EMIR recognition procedure?

EMIR's recognition procedure applies to all non-EU CCPs that provide clearing services to clearing members or trading venues established in the EU. Clearing members established in the EU, i.e. legal persons incorporated under the law of an EU Member-State, will only be able to use non-EU CCPs if they have been recognised under EMIR.

As a consequence, EU clearing members accessing non-EU CCPs through local branches will only be able to continue to do so if those non-EU CCPs are recognised under EMIR. As EMIR only applies to entities established in the EU, this does not apply when EU banking groups access non-EU CCPs through local subsidiaries. In contrast to local branches, these local subsidiaries are not considered as EU clearing members.

This procedure applies to all types of CCP clearing services, irrespective of the type of financial products cleared. As a result, this procedure is not limited to CCPs clearing OTC derivatives.

What are the benefits of being recognised under EMIR?

First, non-EU CCPs recognised in the EU will be able to continue providing services to EU clearing members and trading venues whilst remaining exclusively subject to their domestic legal and supervisory framework. Recognition in the EU does not imply the application of any additional obligation under EU law. Under this approach, the EU fully relies on the application of domestic rules considered as equivalent to EU rules and their enforcement by domestic authorities. In order to guarantee a continuous access to information on the supervision of the CCP, cooperative arrangements ('MoUs') need to be established with domestic authorities.

Second, CCPs recognised in the EU will be able to benefit from the application of the clearing obligation in the EU. This is because EU counterparties subject to the clearing obligation will

be obliged to use either CCPs authorised in the EU or non-EU CCPs recognised under EMIR to fulfil this obligation.

Third, EMIR recognition has implications on the capital treatment of EU banks' exposures to CCPs under the new Basel III rules as transposed in the EU. Only non-EU CCPs recognised under EMIR will meet the conditions necessary to be considered as 'qualified CCPs'. As capital requirements are applied to EU banks on a consolidated basis, this will have an impact on the exposures of branches or subsidiaries of EU banks to non-EU CCPs.

How does the EMIR recognition procedure work?

As provided in Article 25 of EMIR, a CCP established outside the EU may provide clearing services to EU clearing members where it has been recognised by the European Securities Markets Authority (ESMA).

The main conditions for the recognition of a non-EU CCP by ESMA are:

- (i) the European Commission has adopted a positive equivalence decision with regard to the regulatory framework applicable to CCPs in the CCP's home country;
- (ii) the CCP is authorised and subject to effective supervision and enforcement in its home country;
- (iii) the CCP is established or authorised in a third country that is considered as having equivalent systems for anti-money-laundering and combating the financing of terrorism to those of the Union¹;
- (iv) cooperation arrangements have been established between ESMA and the domestic supervisory authorities.

In practice, this means that two processes will need to be run in parallel. On the one hand, ESMA assesses the application for recognition received from non-EU CCPs, and establishes cooperation arrangements with domestic supervisory authorities. On the other hand, the European Commission prepares and adopts equivalence decisions for each foreign jurisdiction.

The adoption of an equivalence decision by the European Commission is by no means a precondition for an application for recognition by ESMA of a non-EU CCP. It is only a precondition to the adoption of a positive recognition decision by ESMA.

What is the process for the adoption of equivalence decisions?

The purpose of equivalence decisions is to verify that the supervisory framework applicable to CCPs in a third-country jurisdiction delivers equivalent results in terms of the soundness and efficiency of the supervision of CCPs. This assessment is not aimed at checking that rules identical to EU rules applicable to CCPs are in place in the third-country. The assessment is

¹ in accordance with the criteria set out in the common understanding between Member States on third-country equivalence under Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

‘outcome-focused’ and takes as much as possible account of the specificities of the regulatory context in the third-country.

For the preparation of equivalence decisions, the European Commission has asked ESMA to provide technical advice on the supervisory framework applicable in third-countries. Technical advice for a first set of countries are expected by 15 June 2013 and, for a second set of countries, by 15 September 2013². The content and the timing for the delivery of this advice neither prejudices the content of the equivalence decision nor of the timing of its adoption. It is not excluded that further advice could be requested from ESMA for additional countries, if necessary.

What is the time line?

Article 89 of EMIR (transitional provisions) provides that a CCP established in a third country that provides clearing services to EU clearing members shall apply for recognition under EMIR within six months of the date of entry into force of EMIR implementing rules (regulatory technical standards).

The regulatory technical standards entered into force on 15 March 2013. Therefore, non-EU CCPs currently providing services to EU clearing members must apply for recognition to ESMA by 15 September 2013.

Within 9 months of the receipt of a complete application, ESMA must make a decision on recognition. Until a decision has been made by ESMA on the application, non-EU CCPs (that have applied for recognition before the 15 September 2013) may continue to provide services to EU clearing members that are already active on those CCPs. In order to guarantee that this transitional regime will continue to apply seamlessly, it is important that ESMA receives applications for recognition by 15 September 2013.

The adoption of an equivalence decision by the European Commission before 15 September 2013 is not a precondition for a CCP to be able to apply for recognition. The equivalence decision is a condition only for the final decision on recognition and may, therefore, be adopted after the receipt of an application.

For any further information, please send an e-mail to MARKT-G2@ec.europa.eu.

² For more information, please refer to:

http://www.esma.local/system/files/european_commission_letter_extending_deadline_for_emir_equivalence_assessments.pdf

Annex: Relevant Articles of EMIR

Article 25

Recognition of a third-country CCP

1. A CCP established in a third country may provide clearing services to clearing members or trading venues established in the Union only where that CCP is recognised by ESMA.

2. ESMA, after consulting the authorities referred to in paragraph 3, may recognise a CCP established in a third country that has applied for recognition to provide certain clearing services or activities where:

(a) the Commission has adopted an implementing act in accordance with paragraph 6;

(b) the CCP is authorised in the relevant third country, and is subject to effective supervision and enforcement ensuring full compliance with the prudential requirements applicable in that third country;

(c) cooperation arrangements have been established pursuant to paragraph 7;

(d) the CCP is established or authorised in a third country that is considered as having equivalent systems for anti-money- laundering and combating the financing of terrorism to those of the Union in accordance with the criteria set out in the common understanding between Member States on third-country equivalence under Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (1).

3. When assessing whether the conditions referred to in paragraph 2 are met, ESMA shall consult:

(a) the competent authority of a Member State in which the CCP provides or intends to provide clearing services and which has been selected by the CCP;

(b) the competent authorities responsible for the supervision of the clearing members of the CCP that are established in the three Member States which make or are anticipated by the CCP to make the largest contributions to the default fund of the CCP referred to in Article 42 on an aggregate basis over a one-year period;

(c) the competent authorities responsible for the supervision of trading venues located in the Union, served or to be served by the CCP;

(d) the competent authorities supervising CCPs established in the Union with which interoperability arrangements have been established;

(e) the relevant members of the ESCB of the Member States in which the CCP provides or intends to provide clearing services and the relevant members of the ESCB responsible for the oversight of the CCPs with which interoperability arrangements have been established;

(f) the central banks of issue of the most relevant Union currencies of the financial instruments cleared or to be cleared.

4. The CCP referred to in paragraph 1 shall submit its application to ESMA.

The applicant CCP shall provide ESMA with all information necessary for its recognition. Within 30 working days of receipt, ESMA shall assess whether the application is complete. If the application is not complete, ESMA shall set a deadline by which the applicant CCP has to provide additional information.

The recognition decision shall be based on the conditions set out in paragraph 2 and shall be independent of any assessment as the basis for the equivalence decision as referred to in Article 13(3).

ESMA shall consult the authorities and entities referred to in paragraph 3 prior to taking its decision.

Within 180 working days of the submission of a complete application, ESMA shall inform the applicant CCP in writing, with a fully reasoned explanation, whether the recognition has been granted or refused.

ESMA shall publish on its website a list of the CCPs recognised in accordance with this Regulation.

5. ESMA shall, after consulting the authorities and entities referred to in paragraph 3, review the recognition of the CCP established in a third country where that CCP has extended the range of its activities and services in the Union. That review shall be conducted in accordance with paragraphs 2, 3 and 4. ESMA may withdraw the recognition of that CCP where the conditions set out in paragraph 2 are no longer met and in the same circumstances as those described in Article 20.

6. The Commission may adopt an implementing act under Article 5 of Regulation (EU) No 182/2011,

determining that the legal and supervisory arrangements of a third country ensure that CCPs authorised in that third country comply with legally binding requirements which are equivalent to the requirements laid down in Title IV of this Regulation, that those CCPs are subject to effective supervision and enforcement in that third country on an ongoing basis and that the legal framework of that third country provides for an effective equivalent system for the recognition of CCPs authorised under third-country legal regimes.

7. ESMA shall establish cooperation arrangements with the relevant competent authorities of third countries whose legal and supervisory frameworks have been recognised as equivalent to this Regulation in accordance with paragraph 6. Such arrangements shall specify at least:

(a) the mechanism for the exchange of information between ESMA and the competent authorities of the third countries concerned, including access to all information requested by ESMA regarding CCPs authorised in third countries;

(b) the mechanism for prompt notification to ESMA where a third-country competent authority deems a CCP it is supervising to be in breach of the conditions of its authorisation or of other law to which it is subject;

(c) the mechanism for prompt notification to ESMA by a third-country competent authority where a CCP it is supervising has been granted the right to provide clearing services to clearing members or clients established in the Union;

(d) the procedures concerning the coordination of supervisory activities including, where appropriate, on-site inspections.

8. In order to ensure consistent application of this Article, ESMA shall develop draft regulatory technical standards specifying the information that the applicant CCP shall provide ESMA in its application for recognition.

ESMA shall submit those draft regulatory technical standards to the Commission by 30 September 2012.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1095/2010.

Article 89

Transitional provisions

[...]

4. Until a decision is made under this Regulation on the authorisation or recognition of a CCP, the respective national rules on authorisation and recognition of CCPs shall continue to apply and the CCP shall continue to be supervised by the competent authority of its Member State of establishment or recognition.

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