

MEMO# 28277

July 17, 2014

EU Regulators Issue Consultation Papers on Clearing Obligation

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TO: DERIVATIVES MARKETS ADVISORY COMMITTEE No. 47-14
CLOSED-END INVESTMENT COMPANY MEMBERS No. 26-14
ICI GLOBAL MEMBERS No. 26-14
INTERNATIONAL MEMBERS No. 25-14
INVESTMENT ADVISER MEMBERS No. 25-14 RE: EU REGULATORS ISSUE CONSULTATION PAPERS ON CLEARING OBLIGATION

On July 11, 2014, the European Securities and Markets Authority (“ESMA”) issued its first round of consultations for central clearing of OTC derivatives within the European Union. [\[1\]](#) The two consultation papers seek views on the draft regulatory technical standards (“RTS”) for the clearing of interest rate swaps (“IRS”) and credit default swaps (“CDS”) under the European Market Infrastructure Regulation (“EMIR”). After the consultation, ESMA will draft its final RTS and submit them to the European Commission for endorsement.

Classes Proposed to be Subject to Clearing Obligation

For IRS, ESMA’s draft RTS propose four classes to be subject to central clearing (on a range of currencies and underlying indices). These classes include: (1) basis swaps; (2) fixed-to-float IRS; (3) forward rate agreements; and (4) overnight index swaps. The following tables provide the classes that are proposed to be subject to the clearing obligation.</p>

Basis swaps class

Type

Reference Index

Settlement Currency

Maturity

Settlement Currency Type

Optionality

Notional Type

Basis

EURIBOR

EUR

28D-50Y

Single currency

No

Constant or Variable

Basis

LIBOR

GBP

28D-50Y

Single currency

No

Constant or Variable

Basis

LIBOR

JPY

28D-50Y

Single currency

No

Constant or Variable

Basis

LIBOR

USD

28D-50Y

Single currency

No

Constant or Variable

Fixed-to-float interest rate swaps class

Type

Reference Index

Settlement Currency

Maturity

Settlement Currency Type

Optionality

Notional Type

Fixed-to-Float

EURIBOR

EUR

28D-50Y

Single currency

No

Constant or Variable

Fixed-to-Float

LIBOR

GBP

28D-50Y

Single currency

No

Constant or Variable

Fixed-to-Float

LIBOR

JPY

28D-50Y

Single currency

No

Constant or Variable

Fixed-to-Float

LIBOR

USD

28D-50Y

Single currency

No

Constant or Variable

Forward rate agreement class

Type

Reference Index

Settlement Currency

Maturity

Settlement Currency Type

Optionality

Notional Type

FRA

EURIBOR

EUR

3D-3Y

Single currency

No

Constant or Variable

FRA

LIBOR

GBP

3D-3Y

Single currency

No

Constant or Variable

FRA

LIBOR

USD

3D-3Y

Single currency

No

Constant or Variable

Overnight index swaps class

Type

Reference Index

Settlement Currency

Maturity

Settlement Currency Type

Optionality

Notional Type

OIS

EONIA

EUR

7D-3Y

Single currency

No

Constant or Variable

OIS

FedFunds

USD

7D-3Y

Single currency

No

Constant or Variable

OIS

SONIA

GBP

7D-3Y

Single currency

No

Constant or Variable

For CDS, ESMA's draft RTS propose to subject CDS on the iTraxx Europe Main and the iTraxx Europe Crossover to the clearing obligation. The table below provides the credit OTC classes proposed to be subject to the clearing obligation.

European untranched index CDS class

Type

Sub-Type

Geographical Zone

Reference Index

Settlement Currency

Series

Maturity

Index CDS

Untranched Index

Europe

iTraxx Europe Main

EUR

11 onwards

5Y

Index CDS

Untranching Index

Europe

iTraxx Europe Crossover

EUR

11 onwards

5Y

Phase-in Period

The clearing obligation will take effect following a phased implementation (proposed range from six months to three years after the entry into force of the RTS) depending on the type of counterparty. ESMA proposes three categories of counterparties for these purposes: (1) clearing members; [\[2\]](#) (2) non-clearing members; [\[3\]](#) and (3) non-financial counterparties above the clearing threshold. AIFs that are not captured by the definition of financial counterparties under EMIR (e.g., EU AIFs marketed in the EU without a passport by non-EU alternative investment fund managers) would be included in Category 1 if they are clearing members meeting the relevant conditions or in Category 2. Third-country entities would determine their categories based on the categories to which they would belong if they were established in the European Union.

The date of application of the clearing obligation would be as follows: (1) six months after entry into force of the RTS for Category 1; (2) 18 months after entry into force of the RTS for Category 2; and (3) three years after entry into force of the RTS for Category 3.

Frontloading

EMIR imposes an obligation to clear the OTC derivatives contracts (relating to a class of OTC derivatives that has been declared subject to the clearing obligation) that are entered into after the notification to ESMA of the authorization of a central counterparty (“CCP”) by the national competent authorities and before the date of application of the clearing obligation. For the period between the notification to ESMA and the publication in the Official Journal of the RTS, ESMA proposes to set the minimum remaining maturity level so that no contract will be subject to frontloading. For contracts entered into between the publication in the Official Journal of the RTS and the date on which the clearing obligation takes effect (the date of application), ESMA proposes to require contracts with more than six months before expiration on the date of application of the clearing obligation to be subject to frontloading.

Jennifer S. Choi
Senior Associate Counsel Securities Regulation

endnotes

[\[1\]](#) European Securities Markets Authority, Consultation Paper, Clearing Obligation under

EMIR (no. 1) (July 11, 2014), available at <http://www.esma.europa.eu/system/files/2014-799.pdf> ("IRS Consultation Paper"); European Securities Markets Authority, Consultation Paper, Clearing Obligation under EMIR (no. 2) (July 11, 2014), available at <http://www.esma.europa.eu/system/files/2014-800.pdf> ("CDS Consultation Paper"). The deadline for comments on the IRS Consultation Paper is August 18, 2014 and on the CDS Consultation Paper is September 18, 2014.

[2] Category 1 (Clearing Members) would include counterparties that, on the date of entry into force of the RTS on the clearing obligation, are clearing members for any of the class of OTC derivatives subject to the clearing obligation under the draft RTS of any CCP authorized to clear at least one of those classes.

[3] Category 2 (Non-Clearing Members) would include any counterparty that falls in neither Category 1 nor Category 3 and includes financial counterparties not included in Category 1 and alternative investment funds ("AIFs") qualifying as non-financial counterparties subject to the clearing obligation ("NFC+") not included in Category 1.