



Alternative Investment  
Management Association

## AIMA UPDATE NOTE

on the progress of the European Commission's draft proposal  
for a Regulation on OTC derivatives, central counterparties  
and trade repositories (EMIR)

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October 2011



## 1. Introduction

This note provides an update for AIMA Members on the European Commission's EMIR proposal, including:

- the progress of the legislation to date;
- the trilogue negotiation process and next steps;
- a summary of changes in the text approved by the Council of Ministers (the Council); and
- a comparison of the texts adopted by the European Parliament (EP) and by the Council.

## 2. Progress to date

On 15 September 2010, the European Commission (the Commission) published its draft proposal for a Regulation on OTC derivatives, central counterparties and trade repositories (the Commission Proposal). Collectively, the various amended versions of the Commission Proposal are commonly referred to as the European Market Infrastructure Regulation or 'EMIR'.

On 24 May 2011, the EP's ECON Committee passed a number of amendments to the Commission Proposal. On 5 July 2011, the EP in plenary session approved the ECON Committee text (the EP Text).

Under the Hungarian and Polish Presidencies of the Council, the Council experts' working group (CWG) has considered a number of different amendments to the Commission Proposal. On 26 September 2011, the CWG forwarded its proposed amendments to the Commission Proposal to the Committee of Permanent Representatives (COREPER), which approved the text with minor amendments. On 4 October 2011, the Finance Ministers of the 27 Member States, sitting as the Council Committee on Economic and Financial Affairs (ECOFIN), approved a final version of their amended text (the Council Text).

## 3. Trilogues and next steps

Under the ordinary legislative procedure, representatives of the Commission, the EP and the Council will now engage in tri-party negotiations (known as "trilogues") to seek to reach agreement on a common text of EMIR. The first trilogue meeting took place on 10 October 2011. Intensive technical and political trilogues are expected to take place in the final quarter of 2011 with all parties hoping to reach a political agreement by the end of the year. This is extremely ambitious.

According to the [press release](#) issued by the Council following the 4 October 2011 agreement, it is still the intention that a final text of EMIR will become effective by 31 December 2012. Many have suggested that this timing is unrealistic given the number of delegated acts and technical standards (secondary implementing legislation) which will have to be drafted, publicly consulted upon and approved by the European Securities and Markets Authority (ESMA) and the European Commission.

## 4. Summary of changes in the Council text

The key changes to the Council Text from the Commission Proposal are set out below. A summary of the Commission Proposal and the EP Text can be found on AIMA's [website](#).

### *Scope*

A major issue within the Council has been the scope of EMIR - whether its provisions will be applicable just to over-the-counter (OTC) derivatives or to all derivatives. Whilst the September 2009 G20 statement calls only for action in respect of OTC derivatives, many have seen the need to apply provisions more widely, to avoid creating a two tier regime and to align the European regime with that in the US (where swaps and futures will be similarly regulated).

The Council Text provides that the clearing obligation (Article 3) and the risk mitigation techniques for uncleared swaps (Article 6) shall be applicable only to OTC derivatives. The Council's view is that, as virtually all exchange-traded derivatives are subject to central clearing in today's market in any case, this is the correct position to take. The new organisational requirements for CCPs (including the collateral and

segregation provisions) will apply to all CCPs clearing all derivatives and other financial instruments. The reporting obligation (Article 7) will be applicable to all derivatives, which will allow market regulators to collect information on the entire derivatives market in a coordinated, comprehensive and consistent manner.

Another area of contention in the Council has been with regard to 'Access to a CCP' (Article 8) and 'Access to a venue of execution' (Article 8a).

Article 8, which provides that a CCP must accept contracts for clearing from any execution venue on a non-discriminatory basis, is only applicable to CCPs which clear OTC derivatives. This has been the agreed position to date between the Council Member States, whereby the 'vertical silo'<sup>1</sup> model of certain exchange and clearing offerings in a number of Member States will not be impacted by the provision. This has been opposed by other Member States (taking a 'buiside' firm interest) who wish to see more competition in trading and clearing services in Europe following the implementation of EMIR.

These issues are expected to be raised again in the discussions surrounding the Commission proposal for a 'Markets in Financial Instruments Regulation' (MiFIR), which contains open access provisions applicable to all financial instruments. Article 8a, which requires venues of execution to provide trade feeds to CCPs, is also only applicable to venues of execution listing OTC derivatives. This provision was first removed and then reinstated immediately prior to the approval of the Council Text on 4 October 2011.

Issues regarding the scope and access provisions of EMIR will likely continue to be debated during the trilogues. The EP Text provides for access to CCPs to be applicable to OTC derivatives only (the same position as is taken in the Council Text) but has provided that access to trade feeds of a venue of execution shall be available on a non-discriminatory basis to CCPs clearing all derivatives. The Commission provides only for non-discriminatory access to CCPs and, again, this is applicable only to those clearing OTC derivatives. The Commission is required to negotiate on the basis of its original proposal in the trilogues; however, it may be willing to concede certain points to the EP and Council in light of its proposals in MiFIR.

#### *Intragroup trades*

The Council has recently dedicated a significant amount of time to reviewing and revising provisions that will exempt intragroup trades from the clearing obligation and, in certain circumstances, the obligations for those trading in uncleared OTC derivatives. It is worth noting that an exemption for intragroup trades is not included in the Commission Proposal, nor is it found in the EP Text. Intragroup trades are first defined in Article 2a and are described separately for financial and non-financial counterparties:

- for a financial counterparty, a derivative is considered an intragroup transaction where it is:
  - (i) entered into with an EU or third country counterparty, each subject to appropriate prudential requirements, included in the same consolidation on a full basis and subject to appropriate centralised risk evaluation, measures and control procedures;
  - (ii) entered into with a counterparty subject to the same institutional protection scheme; or
  - (iii) between credit institutions affiliated to the same central body.
- for a non-financial counterparty, a derivative is considered an intragroup transaction where it is:
  - (i) entered into with an EU or third country counterparty, which is part of the same group;
  - (ii) included in the same consolidation on a full basis; and
  - (iii) the counterparties are subject to appropriate centralised risk evaluation, measurement and control procedures.

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<sup>1</sup> A vertical silo model exists where a group of companies includes both an exchange and a central clearinghouse. The exchange routes all trades to be cleared only with its own central clearing house and the central clearing house only accepts trades from the exchange.

OTC derivative trades meeting these criteria will be fully exempt from the clearing obligation under Article 3. They may also be exempted, in part or in full, from the risk mitigation techniques requirements of Article 6, provided that:

- (i) the counterparties have adequately sound and robust risk management procedures that are consistent with the level of complexity of the derivatives transaction; and
- (ii) there is no current or foreseen practical or legal impediment to the prompt transfer of own funds or repayment of liabilities between the counterparties.

#### *Pension schemes*

Many Member States have expressed concern about the impact of central clearing on pension schemes and the difficulties that pension schemes will have in complying with EMIR. The Council has worked continuously on the definition of a 'pension scheme' (as there is no single EU definition) and what sort of exemption should be provided for them. The definition has widened significantly from earlier versions of the Council Text and now includes:

- institutions for occupational retirement provision, as defined in the IORP Directive<sup>2</sup>;
- legal entities set up for the purpose of the investment of pension schemes (acting solely and exclusively in their interest);
- occupational retirement provision businesses of institutions, referred to in Article 3 of the IORP Directive;
- ring-fenced and separately organised occupational retirement businesses of insurance undertakings; and
- other national institutions set up to provide retirement benefits.

All pension schemes, as well as institutions established for the purpose of providing compensation to members of pension scheme arrangements in the case of a default, will be granted an exemption from the clearing obligation in Article 3, where the contracts are "objectively measurable as reducing investment risks directly related to the financial solvency of pension schemes". Pension schemes will still be required to comply with the reporting obligation and the risk mitigation techniques obligations for uncleared trades.

This exemption is to last for three years following the implementation of EMIR, reduced from the previous proposal of five years. No later than two years after entry into force of EMIR, the Commission, ESMA and the European Insurance and Occupational Pensions Authority (EIOPA) are to assess technical solutions to clearing which address the specific needs of pension scheme arrangements and, if necessary, appropriate regulatory technical standards will be adopted.

The Commission Proposal contained no exemptions for pension schemes and the Commission's position on this issue is unclear. The EP Text contains a similar three year exemption from the clearing obligation but has defined 'pension schemes' to include:

- those established pursuant to the IORP Directive;
- appointed investment managers pursuant to Article 19(1) of the IORP Directive; and
- any other arrangements recognised under national law as schemes established for the purposes of retirement provision.

The EP Text further provides that the Commission may extend the exemption from the clearing obligation beyond the three years where a Commission report concludes that the "undue burden remains disproportionate" and the extension is necessary "in order to ensure resolution of the remaining issues". For uncleared trades, the EP Text also provides that for pension schemes "resilient bilateral collateralisation of derivatives used for risk mitigation shall take account of counterparty creditworthiness. Capital requirements

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<sup>2</sup> Institutions for Occupational Retirement Provision Directive 2003/41/EC

in prudential regulation shall be in line with those of centrally cleared contracts". The question of how pension schemes are defined and what provisions are necessary to avoid placing undue burdens on them are likely to be the subject of significant negotiations during the trilogues.

#### *CCP authorisation and supervision*

In the Council Text, when a CCP is approved under EMIR to provide clearing services, the CCP must submit an application for authorisation to its competent authority. A college of supervisors (the College), comprising ESMA, relevant competent authorities (who oversee clearing members, venues of executions, etc.) and central banks, shall also be established to provide ongoing supervision of the CCP and exchange information related to the CCP. The Commission Proposal includes that a competent authority may only approve the authorisation of a CCP where it receives a positive opinion that authorisation should be granted from the College. This has caused concern for many Member States, who fear losing the ability to authorise their own existing national CCPs, since such a decision may be blocked by other Member States, represented in the College through their competent authorities. Immediately prior to the 4 October 2011 meeting, the Council reached a compromise whereby a competent authority must review an opinion of the College but is not required to reject the application on presentation of a negative opinion of the College. However, the competent authority must reject a CCP's application for authorisation where "all the members of the College, excluding the authorities of the Member State of establishment of the CCP, reach a joint opinion by mutual agreement that the CCP should not receive authorisation".

The EP Text provides that a competent authority may only provide authorisation to a CCP following a positive opinion of the College, the opinion being agreed among a simple majority of members.

#### *Third Country issues*

The third country provisions in EMIR have proved to be some of the most controversial and the issues have been the subject of great debate in the Council. The Council has introduced a number of important new provisions into the Council Text approved by the CWG.

The first extends the clearing obligation (Article 3) not only to trades between EU counterparties and an EU counterparty and a third country counterparty, but to trades between two non-EU counterparties where:

- the contract has a direct, substantial and foreseeable effect within the EU; or
- it is necessary or appropriate to prevent the evasion of any provisions of EMIR.

This provision mirrors similar language in Article 722(d) of the US Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. It additionally creates a wide extraterritorial scope to EMIR and the terms of the Article as drafted will be a concern to many non-EU firms who may struggle to obtain certainty on whether the obligations of EMIR will apply to them.

The second amended provision is a new Article 9a on International Coordination. This is designed to address the issue that arises where an EU counterparty deals with a non-EU counterparty and the derivative contract may potentially be subject to both the EU regime and a third country regime, with possibly conflicting or duplicative obligations for the counterparties. Article 9a provides that the Commission may adopt an implementing act which declares that the legal, supervisory and enforcement arrangements of a third country are equivalent to the requirements under EMIR. Thereafter, the parties may consider their obligations under EMIR fulfilled, provided that:

- the legal framework of the third country is being effectively applied and enforced;
- the legal framework of the third country is applied and enforced in an equitable and non-distortive manner; and
- there is no risk of an adverse effect on the financial market within the EU.

The third new provision amends Article 23 (Recognition of a CCP). Whilst the Commission has proposed that a third country CCP must be recognised to provide clearing services to "entities" established in the EU, the Council Text states that the third country CCP must be recognised to provide clearing services to "clearing

members or venues of execution". This simplifies the issue of third country recognition by only requiring recognition for providing clearing services to clearing members and trading venues in the EU and not all trading entities, such as banks and investment funds.

The decision on recognition shall be made by ESMA after consultation with a college comprising various relevant competent authorities and central banks. This decision will be based on whether the CCP is (i) authorised and subject to effective supervision and enforcement; and (ii) in full compliance with the prudential requirements applicable in that third country. ESMA would also have to adopt an implementing act determining that:

- (i) the legal and supervisory arrangements of the third country are equivalent to those in EMIR;
- (ii) third country CCPs are subject to effective supervision and enforcement; and
- (iii) the third country provides for effective equivalent recognition of EU authorised CCPs.

A cooperation arrangement must also be agreed between ESMA and the third country competent authority that provides for the exchange of information about authorisations of third country CCPs.

In a statement at the end of the Council Text it states: "The Council notes that the drafting of third-country provisions, namely Articles 9a, 23, 62 and 63, requires further work, which will be completed in the context of negotiations with the European Parliament". The resolution of these issues will be somewhat dependent on the final rules implemented by the SEC and CFTC in the US. The EP Text is substantially different from and more onerous than that of the Council regarding the recognition of third country CCPs. It does not, however, contain any provisions similar to the addition in the Council Text at Article 3. We expect there to be significant negotiation on third country issues during the trilogues.

## 5. Conclusion

AIMA welcomed the Commission's Proposal when published, as we believed that it reflected the G20 commitments on clearing and reporting on OTC derivatives and provided comprehensive rules, which would reduce risk and enhance transparency in OTC derivative markets.

We consider that the majority of amendments put forward in the Council Text and by the Parliament's ECON Committee, are largely either neutral or positive. The amendments contain much which would improve on the Commission Proposal and alleviate many of our concerns. For example, in the approved Council Text we are pleased with the ability for EU counterparties dealing with non-EU counterparties to be considered in compliance with EMIR if they meet the obligations of an effective and equivalent third country regime. There are also improvements in the way full segregation is defined in the Council text.

The one area where we remain dissatisfied with the final Council Text is that of the composition of risk committees. There, unlike the EP, the Council has taken an approach which does not guarantee any buy-side presence on the risk committees. This issue was not discussed thoroughly during the CWG discussions and will be revisited in the trilogues as the Parliament has taken a view that a risk committee must include buy-side representation and that clearing members may not hold a majority of seats on the committee. For a more detailed comparison of the various areas of the EP and Council texts, please see the Annex.

Now that the European Institutions have finalised their respective amendments to the Commission Proposal, there remains much work to be done if we are to ensure that the final agreed text of EMIR addresses both the political questions associated with mandating the use of services provided by new and large systemically important institutions and also the technical issues of importance to market users as they begin to plan to clear and report trades from 2013. It is crucial that agreement be found on the issue of third countries and the EU and US officials will, in particular, need to continue to engage in intense dialogue.

If members have any questions about the Council Text, please contact [Jiří Król](#) or [Daniel Measor](#).

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## Annex

### Comparison of EP and Council Texts in respect of AIMA’s main concerns

In December 2010, AIMA published a Position Paper on the Commission Proposal, in which we identified a number of key areas of concern. We set out below AIMA’s key points and the positions taken by the EP and by the Council in their approved position in respect of each of these issues.

#### (a) Scope and definitions

**AIMA’s key point:**

- We support clearing of OTC derivatives and believe the requirements should be applied as broadly as appropriate.

EP Text	Council Text
<p>Under the EP Text, the clearing obligation, non-discriminatory access provision and requirements for uncleared trades will all apply to derivatives, as defined in MiFID, traded over-the-counter (OTC).</p> <p>Despite pressure to exclude particular classes of foreign exchange derivative contracts, this was not taken up in the EP Text. The EP Text does, however, state at Recital 12b that “for certain classes of derivatives, involving exchange of principal, such as foreign exchange, settlement risk may be the predominant risk, which is already addressed through existing market infrastructure. This should be taken into account when considering which classes of derivatives should be mandated for central clearing.”</p> <p>The clearing obligation would not apply to intragroup trades where the contracts are ‘justified for economic reasons’, where the contract does not increase systemic risk in the financial system and where there are no legal restrictions to capital flows between the undertakings.</p> <p>Pension schemes, which are specifically defined in the EP Text definitions, must comply with the clearing obligations as financial counterparties, except in so far as the posting of liquid collateral would result in an undue burden on the investor due to asset conversion requirements. Their obligation to clear eligible contracts is delayed for three years following implementation of EMIR. This may be extended by the Commission beyond the three years should a Commission report conclude that the “undue burden remains disproportionate” and the extension is necessary “in order to ensure resolution of the remaining issues”.</p>	<p>In the Council, there has been significant debate as to whether EMIR should apply to OTC derivatives or to all derivatives, wherever they are traded. The Council Text provides that the clearing obligation for financial and non-financial counterparties, risk mitigation techniques for uncleared trades and access requirements for CCPs and trade execution venues shall only be applicable to OTC derivatives. The reporting obligation and the requirements applicable to CCPs (including the collateral segregation provision) shall apply to derivatives traded either OTC or on a regulated market.</p> <p>Intragroup transactions are excluded from the clearing obligation, where:</p> <p><u>for a financial counterparty</u>, the transaction is</p> <ul style="list-style-type: none"> <li>(i) entered into with an EU or third country counterparty, each subject to appropriate prudential requirements, included in the same consolidation on a full basis and subject to appropriate centralised risk evaluation, measures and control procedures;</li> <li>(ii) entered into with a counterparty subject to the same institutional protection scheme; or</li> <li>(iii) between credit institutions affiliated to the same central body; or</li> </ul> <p><u>for a non-financial counterparty</u>, the counterparties are part of the same group, included in the same consolidation on a full basis and the counterparties are subject to appropriate centralised risk evaluation, measurement and control procedures. Intragroup trades may also either be totally or partially exempted from the risk mitigation techniques requirements provided that:</p> <ul style="list-style-type: none"> <li>(i) the counterparties have adequately sound and robust risk management procedures that are consistent with the level of complexity of the derivative</li> </ul>

	<p>transaction; and                  (ii) there is no current or foreseen practical or legal impediment to the prompt transfer of own funds or repayment of liabilities between the counterparties.</p> <p>Pension Scheme arrangements including: (i) institutions for occupational retirement provision, as defined in the IORP Directive; (ii) legal entities set up for the purpose of investment of pension schemes’ assets (acting solely and exclusively in their interest); (iii) occupational retirement provision businesses of institutions; (iv) ring-fenced and separately organised occupational retirement businesses of insurance undertakings; and (v) other national institutions set up to provide retirement benefits, shall not be subject to the clearing obligation for three years following entry into force of EMIR where the contracts are “objectively measurable as reducing investment risks directly related to the financial solvency of pension schemes”. The exemption shall also apply to institutions established to provide compensation to members of a pension scheme in case of default. No later than two years after entry into force of EMIR, the Commission, ESMA and EIOPA shall assess the technical solutions to clearing that address the specific needs of pension scheme arrangements and, if necessary, shall adopt further regulatory technical standards.</p>
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(b) The clearing obligation

<p><b>AIMA’s key points:</b></p> <ul style="list-style-type: none"> <li>• Under the ‘top down’ approach, ESMA should consult publicly on any class of derivatives which it proposes for the clearing obligation.</li> <li>• Those classes of contract which are eligible for clearing but for which no CCP is yet authorised or recognised to clear should not be subject to the mandatory clearing obligation.</li> </ul>
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EP Text	Council Text
<p>The EP Text provides that financial counterparties and certain non-financial counterparties<sup>3</sup> that conclude a contract with other financial/non-financial counterparties (including third country counterparties) shall clear their OTC derivative contracts if the contract is deemed ‘eligible’.</p> <p>A contract will be considered eligible if:</p>	<p>The Council Text provides that contracts declared subject to the clearing obligation must be cleared if entered into by financial counterparties and certain non-financial counterparties<sup>4</sup>; or where one of those counterparties enters into the trade with a third country entity that would be subject to the clearing obligation if it were established in the EU. The clearing obligation will also apply to eligible trades between two third country entities, where the contact has a</p>

<sup>3</sup> Certain non-financial counterparties will not be required to clear eligible OTC derivatives contracts if their rolling average position, objectively measurable as directly linked to the hedging of commercial or treasury financing activity, for 50 business days does not exceed a threshold that will be determined by ESMA and the Commission.

<sup>4</sup> The Council Text contains a similar threshold to the ECON Text but the relevant time period under which the position is maintained is 30 days over a three month period.

<ul style="list-style-type: none"> <li>• an authorised CCP (or recognised third country CCP) is currently clearing a class of derivatives and ESMA deems the contract ‘eligible’ (the Bottom-up approach); or</li> <li>• ESMA, on its own initiative, identifies a class of derivatives which it believes should be subject to the clearing obligation (the Top-down approach).</li> </ul> <p>Under each approach, ESMA shall conduct a public consultation and consult the European Systemic Risk Board (ESRB) and, where relevant, competent authorities of third countries. Under the Top-down approach, if no CCP is available to clear the class of derivatives, ESMA shall publish a “call for development” of proposals to clear the class of derivatives.</p> <p>The EP Text states that ESMA shall base its decision as to which contracts will be ‘eligible’ on (i) the reduction of systemic risk in the financial system; (ii) the liquidity of contracts; (iii) the availability of fair, reliable and generally accepted pricing sources; and (iv) international consensus.</p> <p>The clearing obligation may be applicable to different counterparties or classes of counterparties at a range of dates after the clearing obligation takes effect.</p> <p>To achieve international consistency, the Commission may seek a mandate to negotiate with third countries regarding making EMIR and a third country’s legislation consistent.</p> <p>Classes of contract subject to the clearing obligation shall be recorded in a public register maintained by ESMA.</p>	<p>“direct, substantial and foreseeable effect within the EU” or “where such obligation is necessary or appropriate to prevent the evasion of any provisions of this regulation”.</p> <p>The Council Text contains a Bottom-up approach and a Top-down approach in the same manner as the EP Text.</p> <p>The clearing obligation may be applicable to different categories of counterparty at different dates. Contracts entered into before the clearing obligation takes effect may also be required to be cleared if they have greater than a minimum remaining maturity (“front loading”).</p> <p>The Council Text states that ESMA shall base its decision as to which contracts will be subject to the clearing obligation, with an overarching aim of reducing systemic risk, on: (i) the degree of standardisation of the class of derivatives (contractual terms and operational processes); (ii) the volume and liquidity of the class of derivatives; and (iii) the availability of fair, reliable and generally accepted pricing sources. When making its decisions, ESMA may additionally “take into consideration the anticipated impact on the level of counterparty credit risk between counterparties as well as the impact on competition across the Union”.</p> <p>In determining which categories of counterparty shall be subject to the clearing obligation and whether the contract will be front loaded, ESMA shall look at: (i) the expected volume of relevant contracts; (ii) whether one or more CCPs already clear the same class of derivatives; (iii) the ability of relevant CCPs to handle the expected volume; (iv) the type and number (or expected number) of active counterparties in the class of derivatives; (v) the time needed by a counterparty to put in place arrangements to clear a class of derivatives with a CCP; and (vi) the risk management, legal and operational capacity of the counterparties. The Commission will adopt implementing technical standards determining the minimum remaining maturity for front loaded contracts.</p> <p>Classes of contract subject to the clearing obligation shall be recorded in a public register maintained by ESMA.</p>
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(c) Access to CCPs and trading venues

AIMA's key points:

- A CCP must maintain non-discriminatory access for any class of contract for which it is authorised to clear, wherever that contract is executed.
- A CCP should equally have non-discriminatory access to venues of execution for the purposes of obtaining prices and closing out positions.

EP Text	Council Text
<p>The EP Text provides for access to CCPs for clearing on a transparent, fair and non-discriminatory basis, regardless of the venue of execution. Execution venues must comply with operational, technical, legal, access and risk management requirements established by the CCP.</p> <p>A trading venue which seeks CCP access but which is denied such access must be provided with a fully reasoned response to its request and, if there are disputes between competent authorities regarding access, the trading venue may apply to ESMA to settle any dispute.</p> <p>A CCP shall have the right to non-discriminatory access to the data feed of any particular trading venue and access to any relevant settlement system that it needs for the performance of its duties.</p>	<p>The Council Text contains the same non-discriminatory access to CCPs provision as the EP Text but clarifies that this access is subject to compliance with operational and technical requirements of the CCP.</p> <p>A trading venue which seeks CCP access but which is denied such access must be provided with a fully reasoned response to its request. The competent authority of the trading venue and the CCP may only deny access to the CCP where it would threaten the smooth and orderly functioning of the markets.</p> <p>Venues of execution are required to provide trade feeds on a non-discriminatory and transparent basis to all authorised and recognised CCPs. The trading venue can only deny such access if it would (i) require interoperability; or (ii) threaten the smooth and orderly functioning of the markets and the trading venue shall be required to provide a fully reasoned response to the CCP in that instance.</p>

(d) The reporting obligation

AIMA's key points:

- All financial and non-financial market participants should be required to report the details of all cleared and uncleared derivative trades to trade repositories.
- Such reporting should be undertaken by the CCP where possible.

EP Text	Council Text
<p>The EP Text requires reporting of all derivative trades (whether cleared or not), when entered into or materially modified, novated or terminated, to a trade repository. ESMA is empowered to examine and conduct a public consultation on whether retrospective reporting obligations can be introduced.</p> <p>All reporting shall be based, where possible, on</p>	<p>The Council Text requires reporting of all derivative trades (whether cleared or not) by counterparties or a CCP when they have concluded, modified or terminated a contract.</p> <p>Reporting shall include all derivatives entered into on or after the date on which EMIR takes effect and all derivatives that are outstanding as at that date.</p>

<p>international industry open standards.</p> <p>The reporting obligation will be undertaken by a CCP where it is cleared by a CCP. Where it is not cleared, a counterparty may delegate the obligation to the other counterparty or a third party, ensuring that details are not reported twice. Reporting may be undertaken by a trade compression operator where the contracts are subject to trade compression.</p> <p>Reports shall contain at least details of the parties to the contract (and their underlying beneficiaries, where applicable), the main characteristics of the contract and a unique contract identifier.</p> <p>Where a trade repository is not available, counterparties shall report details of their trades to ESMA.</p>	<p>A counterparty or a CCP may delegate its reporting obligation. Counterparties and CCPs shall ensure details are reported without duplication.</p> <p>Reports shall contain at least the details of the parties to the contract and the main characteristics of the contract (including the type, underlying maturity and notional value).</p> <p>Where a trade repository is not available, counterparties shall report details of their trades to ESMA.</p>
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(e) Contracts not cleared by CCP

<p><b>AIMA's key points:</b></p> <ul style="list-style-type: none"> <li>• Counterparties to uncleared trades should be required to exchange appropriate amounts of collateral.</li> <li>• Clients must be offered the option of segregation of their collateral with independent third party custodians.</li> </ul>
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EP Text	Council Text
<p>The EP Text provides that those financial and certain non-financial counterparties that would be subject to the clearing obligation for a contract, but for which a contract is not cleared by a CCP, shall have appropriate prudential procedures and arrangements to measure, monitor and mitigate operational, market and credit risk, including by exchange of collateral or capital backing commensurate with the risk.</p> <p>Parties must offer their counterparties the option of segregation of initial margin at the outset of the contract.</p> <p>Competent authorities and ESMA shall aim to prevent regulatory arbitrage between cleared and uncleared transactions and reflect risk transfers arising from derivative contracts.</p> <p>For Pension Schemes, bilateral collateralisation shall take account of counterparty creditworthiness and applicable capital requirements shall be aligned with those for centrally cleared contracts.</p> <p>ESMA shall monitor activities in uncleared derivatives</p>	<p>The Council Text provides that financial and certain non-financial counterparties shall have appropriate procedures and arrangements to measure, monitor and mitigate operational, market and credit risk, including by (i) timely confirmation of the terms of a derivative contract; (ii) robust, resilient and auditable process for reconciling portfolios, managing associated risks, identifying and resolving disputes between the parties and monitoring the value of contracts; and (iii) the timely, accurate and appropriate exchange of collateral. Financial counterparties shall hold appropriate and proportionate amounts of capital (to be determined in regulatory technical standards) to manage risk not covered by exchange of collateral.</p> <p>If requested, parties must distinguish in accounts (including as separately recorded in their own accounts), in accordance with their agreement, the assets provided by the other party (i.e., segregation of assets).</p> <p>Obligations for uncleared trades shall not apply to certain intragroup transactions (see above).</p>

to identify classes of contracts that may pose systemic risk and, where it does so, take action to prevent further accumulation of contracts in such class.	
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**(f) CCP authorisation and supervision**

<p><b>AIMA’s key points:</b></p> <ul style="list-style-type: none"> <li>• CCPs should be subject to appropriate authorisation conditions.</li> <li>• CCPs should be well supervised by an appropriate authority.</li> </ul>
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EP Text	Council Text
<p>A CCP shall apply to the competent authority of the Member State in which it is established for authorisation, if it has adequate access to central bank or commercial bank liquidity to perform its services and activities. Authorisation is granted if the competent authority approves the application and ESMA and a college of authorities (including other competent authorities and central banks) deliver a positive opinion that the CCP is safe to operate in the EU. Authorisation is effective for the entire territory of the EU.</p> <p>CCPs shall have initial capital of at least EUR 10 million.</p> <p>The competent authority in the Member State of establishment shall be responsible for ongoing supervision of a CCP.</p>	<p>A CCP shall apply to the competent authority of the Member State in which it is established for authorisation. Authorisation is granted if the competent authority approves the application, after considering an opinion of a college comprising ESMA, the European System of Central Banks (ESCB), other competent authorities and central banks. A CCP’s application will be rejected where “all the members of the college, excluding the authorities of the Member State of establishment of the CCP, reach a joint opinion by mutual agreement that the CCP should not receive authorisation”.</p> <p>CCPs shall have initial capital of at least EUR 5 million.</p> <p>The competent authority in the Member State of establishment shall be responsible for ongoing supervision of a CCP.</p>

**(g) Third country CCPs**

<p><b>AIMA’s key points:</b></p> <ul style="list-style-type: none"> <li>• It is important that the EU should be able to recognise third country CCPs such that EU counterparties have a competitive choice of available CCPs, especially where trading occurs outside of the EU.</li> <li>• Third country CCPs should be recognised if they meet standards broadly equivalent to EMIR.</li> </ul>
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EP Text	Council Text
<p>The EP Text requires third country CCPs to gain recognition from ESMA to provide clearing services to entities established in the EU. Recognition is first subject to the CCP authorisation conditions laid down in Articles 10 to 16 and third country CCPs shall be subject to a review process of similar rigueur to the</p>	<p>The Council Text requires third country CCPs to gain recognition from ESMA to provide clearing services to (i) clearing members; and (ii) venues of execution established in the EU.</p> <p>ESMA may make a decision to grant recognition to a</p>

<p>one EU CCPs are subject to. Second, the third country CCP must be subject to effective supervision and enforcement in the third country and be subject to legally binding requirements, which are equivalent to the requirements of EMIR (including risk management standards). Third, third countries in which the CCPs are established must meet the FATF AML standards, have an OECD Model Tax Convention with the relevant EU Member State, have a legal framework that does not discriminate against EU legal entities, allows reciprocal access conditions for EU based CCPs and provides for mutual recognition and the conditions imposed on EU entities preserve a level playing field with third country entities.</p> <p>The Commission may grant an exemption from the authorisation conditions and procedures if this is done on a reciprocal basis with the third country that allows EU-established CCPs to gain access to that third country.</p>	<p>third country CCP. The decision on recognition shall be made by ESMA after consultation with a college comprising various competent authorities and central banks. The decision will be based on whether the CCP is: (i) authorised in and subject to effective supervision and enforcement; and (ii) in full compliance with the prudential requirements applicable in that third country. ESMA must also adopt an implementing act determining that: (i) legal and supervisory arrangements of the third country are equivalent to those in EMIR; (ii) third county CCPs are subject to effective supervision and enforcement; and (iii) the third country provides for effective equivalent recognition of EU authorised CCPs. A cooperation arrangement must also be agreed that provides for the exchange of information about authorisations of third country CCPs.</p> <p>Counterparties subject to the clearing and reporting obligations and obligations for uncleared trades may be deemed to have fulfilled their obligations when trading with third country counterparties where the trades are cleared subject to a third country's legal regime, recognised by the Commission as being equivalent to EMIR. The third country framework must also be: (i) effectively applied and enforced; and (ii) equitable and non-distortive, and there must be no risk of an adverse effect on the financial markets within the EU.</p>
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(h) Risk committees and board participation

<p>AIMA's key points:</p> <ul style="list-style-type: none"> <li>• Risk committees play an important role in ensuring the safe operation of a CCP.</li> <li>• It is essential that clients are represented on the risk committee, not subject to a mere consultation mechanism.</li> <li>• Clearing members should not have a majority position on the Risk Committee.</li> </ul>
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EP Text	Council Text
<p>The EP Text provides that CCP risk committees shall be composed of representatives from clearing members, clients of clearing members, independent experts and the competent authority of the CCP. No one group may represent a majority of the committee. The committee will be chaired by an independent expert who reports directly to the board.</p> <p>The risk committee's role will be to advise the board on arrangements affecting risk management of the CCP, including changes to the risk model, default procedures and accepting new clearing members or classes of financial instruments for clearing.</p>	<p>The Council Text is little changed from the Commission Proposal. The risk committee may now invite external independent experts and independent members of the board to attend the risk committee meetings in a non-voting capacity.</p> <p>CCPs shall allow clients of the clearing members to attend risk committee meetings in a non-voting capacity or, alternatively, establish an appropriate consultation mechanism to ensure clients' interests are adequately represented.</p> <p>The CCP's board shall comprise at least one third and no less than two, independent board members.</p>

Reasonable efforts should be made to consult the risk committee in emergency situations.	
CCPs shall have a board, which must include representation of the clients of clearing members.	

(i) Segregation and portability

<p>AIMA's key points:</p> <ul style="list-style-type: none"> <li>• Full segregation of assets and positions should be offered to clients at reasonable cost.</li> <li>• The final EMIR text should be very clear on what 'segregation' is.</li> <li>• Segregation must be effective under all Member States' insolvency laws.</li> </ul>
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EP Text	Council Text
<p>The EP Text provides for identification and segregation of assets and positions by the CCP, through the use of records and accounts, between:</p> <ul style="list-style-type: none"> <li>• the CCP and a clearing member;</li> <li>• a clearing member and other clearing members; and</li> <li>• a clearing member and a third party who holds assets and funds.</li> </ul> <p>The clearing member shall distinguish, in separate accounts with the CCP, the positions of a clearing member from its clients.</p> <p>A client shall also have positions distinguished in separate accounts with the CCP ('full segregation') but shall be given the possibility to have positions recorded in omnibus accounts upon request. CCPs and clearing members must disclose the costs and level of protection provided by each option.</p> <p>Records must be kept to identify the assets in relation to each account.</p> <p>Full segregation shall ensure that positions and collateral can be transferred to other clearing members upon a clearing member's default.</p> <p>Member States will ensure their national insolvency laws provide derogations sufficient to allow EMIR's segregation objectives and requirements to be met.</p>	<p>The Council Text provides that the CCP shall keep records and accounts enabling it to 'distinguish in accounts' the assets (i.e., collateral or equivalent assets or proceeds of realisation of collateral) and positions of :</p> <ul style="list-style-type: none"> <li>• the CCP and a clearing member;</li> <li>• a clearing member from other clearing members; and</li> <li>• clients of a clearing member from the clearing member.</li> </ul> <p>Clearing members shall offer to keep records and accounts for clients to enable clearing members to distinguish in accounts held with the CCP the asset and positions of a client from those of other clients ('individual client segregation'). The CCP shall also offer more detailed levels of segregation.</p> <p>For individual client segregation, excess margin beyond the client's requirements will also be distinguished and not exposed to losses in other accounts. CCPs and clearing members must disclose the costs and level of protection provided by each option. Segregation must be offered under reasonable commercial terms.</p> <p>The CCP shall have a right of use related to margin and default fund contributions collected via title transfer collateral arrangement, provided this is foreseen by the operating rules and the right is publicly disclosed.</p> <p>Distinguishing assets and positions is achieved if:</p> <ul style="list-style-type: none"> <li>• assets and positions are recorded in separate accounts;</li> <li>• netting of positions recorded on different accounts is prevented; and</li> <li>• assets covering recorded positions are not exposed to losses connected to positions recorded in other accounts.</li> </ul>

(j) Participation requirements and ownership

AIMA's key points:

- CCP participation by clearing members should be open to any type of firm as long as they meet certain risk-based criteria.
- Wide participation by many clearing members should be encouraged.

EP Text	Council Text
<p>The EP Text states that a CCP shall establish criteria for admissible clearing members that are non-discriminatory, transparency and objective, considering whether the proposed participant has sufficient financial resources and operational capacity to meet their obligations. Further, financial institutions cannot be restricted from being clearing members in uncompetitive or unreasonable ways.</p> <p>Clearing members will be responsible for monitoring and collecting information on their clients but are not permitted to set criteria that would be discriminatory.</p> <p>A potential clearing member may be refused, even if they meet the applicable financial resources and operational capacity criteria, if it is justified in writing and based on a comprehensive risk analysis.</p>	<p>The Council Text retains the text of the Commission Proposal, except that categories of admissible clearing members and the relevant criteria shall be set according to the types of products cleared. The admission criteria shall be non-discriminatory, transparent and objective to ensure fair and open access to the CCP.</p> <p>Decisions on admitting new clearing members can only be made after seeking the advice of the established risk committee.</p>

(k) Collateral requirements

AIMA's key points:

- CCPs should be limited to accepting highly liquid collateral with minimal credit and market risk.
- Appropriate haircuts to value should be given to reflect potential reduction in value.

EP Text	Council Text
<p>The EP Text retains much of the Commission Proposal but includes a provision whereby highly liquid collateral shall include cash, gold, government and high quality corporate bonds. In the case of non-financial counterparties, CCPs may accept bank guarantees.</p> <p>The level and type of collateral shall be set out in draft regulatory technical standards developed by ESMA in consultation with the ESCB and EBA and approved by the Commission. These shall be regularly revised to reflect market conditions.</p>	<p>The Council Text retains the text of the Commission Proposal, which requires that CCPs accept only highly liquid collateral with minimal credit and market risk.</p>