EMIR and MiFID2/MiFIR: Update on recognition procedures for non-EU markets and CCPs

August 2015

CLIFFORD
CHANCE

Contents

This document is not intended to be comprehensive or to provide legal advice. For more information, speak to your usual Clifford Chance contact or one of the lawyers named below.

Amendments to definition of OTC derivatives under EMIR

Planned changes to EMIR should help end the anomaly under which all non-EU exchange-traded derivatives (ETD) are treated as “OTC derivatives” for the purposes of EMIR.

The recently agreed Regulation on Securities Financing Transactions (SFTR) will amend the definition of “OTC derivatives” in Article 2(7) EMIR and will introduce a new procedure for recognising non-EU markets as equivalent for these purposes (new Article 2a EMIR).

The current definition of OTC derivatives in EMIR causes difficulty to market participants trading in non-EU ETD.

- Article 2(7) of EMIR currently provides that derivatives are treated as “OTC derivatives” for the purposes of EMIR except where they are executed on an EU regulated market or a non-EU market considered equivalent to a regulated market in accordance with Article 19(6) MiFID1.
- Article 19(6) MiFID1 provides (for the purposes of the appropriateness requirement) that non-EU markets are considered equivalent to a regulated market if they comply with equivalent requirements to those established under Title III MiFID1 and provides for the Commission to publish a list of equivalent markets.
- ESMA has stated in its Q&A that a market cannot be considered equivalent for the purposes of EMIR unless it is included on a list published by the Commission, but the Commission has not yet listed any non-EU markets and, as a result, market participants are required to treat all non-EU ETD as “OTC derivatives”.
- For example, corporates and other EU and non-EU "non-financial counterparties" have to include positions in non-EU ETDs when determining whether their total groupwide outstanding "non-hedging" OTC derivative transactions are over the clearing threshold (Article 10 EMIR).

The new procedure introduced by SFTR should give the Commission a flexible tool for recognising non-EU futures and derivatives exchanges under EMIR.

- The Commission will be able to adopt implementing acts designating non-EU markets as equivalent for these purposes if:
  - The market complies with legally binding requirements which are equivalent to the requirements laid down in Title III of MiFID1 (or after its repeal and replacement in 2017, the successor provisions in MiFID2/MiFIR); and
  - The market is subject to effective supervision and enforcement in that third country on an ongoing basis.
- The Commission will be able to designate markets individually (it will not have to determine that the entire non-EU regime regulating markets is equivalent), there is no provision in the amended regime requiring reciprocal treatment for EU markets and markets do not need to apply for recognition.

The new procedure is likely to be available early in 2016 and, if the Commission acts quickly, the first designations could be made before the implementation of the first clearing mandate under EMIR (expected in April 2016).

- Next steps: review of the SFTR text by lawyer-linguists, approval by the European Parliament in plenary (set for 27 October 2015), endorsement by the Council, translation into official EU languages, signature by the Parliament and Council and publication in the Official Journal (entry into force will be 20 days after publication).
- But even if the SFTR enters into force in early 2016, the Commission has to act by the “examination procedure” in conjunction with the European Securities Committee to adopt acts designating non-EU markets, meaning that there could be some delay in adopting the first designations.
- Designating relevant markets before the EMIR clearing mandate takes effect would address any residual concern that ETD traded on those markets might be treated as OTC derivatives falling within the scope of the mandate if they meet the characteristics stated in the RTS for the clearing mandate under EMIR.

MiFID2/MiFIR provide separate procedures for recognition of non-EU markets

There are two main processes for recognising non-EU markets as equivalent to EU markets under MiFID2/MiFIR.

For some purposes, MIFID2/MiFIR cross-refer to the process in the Prospectus Directive for determining when non-EU markets are equivalent.

- This is relevant for determining when:
  - EU investment firms may satisfy the mandatory on venue trading requirement for shares by concluding transactions on a regulated market authorised in a non-EU state.
  - It is also relevant for determining when appropriateness requirements are waived for EU investment firms conducting execution only transactions in certain shares and bonds admitted to trading on a regulated market authorised in that third country.
- However, this process has not yet been used and requires a competent authority in a member state to act to initiate the equivalence determination.

MiFIR provides a separate process to determine when market participants can comply with the trading mandate for OTC derivatives by executing the transaction on a non-EU market.

- The same process is also used to determine when non-EU ETD are “exchange traded derivatives” subject to the rules on indirect clearing under MiFIR and when non-EU trading venues can request access to an EU central counterparty (CCP).

In addition, there is a separate procedure for determining when non-EU markets and CCPs can make use of the rights of access to EU CCPs, trading venues and benchmarks.

The Commission has not published details of the likely timing for consideration of equivalence assessments under MiFID2/MiFIR.

The following tables identify the processes for determining when non-EU markets and CCPs are equivalent to EU markets and CCPs under EMIR and MiFID2/MiFIR.

The tables also summarise the benefits and consequences of, and the process and criteria for, an equivalence determination.

EMIR

Equivalence assessment	Benefits/consequences	Process and criteria	Comments
Amended Article 2(7) and new Article 2a EMIR will provide a new procedure for recognition of third country markets as equivalent to recognised markets (as amended by SFTR - not yet in force).	Where a third country market is treated as equivalent to a regulated market, derivatives executed on that market are not "OTC derivatives" for the purposes of EMIR (e.g. for the purposes of determining whether the clearing obligation applies under Article 4 EMIR or computing the clearing threshold under Article 10 EMIR).	The Commission adopts an implementing act determining that: ■ a third-country market complies with legally binding requirements which are equivalent to the requirements laid down in Title III of Directive 2004/39/EC [MIFID] and ■ it is subject to effective supervision and enforcement in that third country on an ongoing basis. The Commission acts in accordance with the examination procedure referred to in Article 86(2) EMIR.	No reciprocity requirement. Assessment is of individual markets not regulatory regimes as a whole. Amended procedure is being introduced by SFTR (expected to be in force end 2015). It is understood that the Commission does not propose to make any determinations with respect to derivatives exchanges under the provisions previously referred to in Article 2(7) EMIR. There will still be a mismatch between the definition of exchange traded derivatives under MiFIR and the definition of OTC derivatives under EMIR in relation to derivatives executed on non-EU markets (see below).
Article 25 EMIR provides a procedure for recognising third country CCPs as equivalent (in force)	Where a CCP is recognised as equivalent: ■ the CCP is permitted to provide clearing services to EU clearing members and trading venues (Article 25(1) EMIR and Article 38(1) MiFIR); ■ counterparties subject to the clearing obligation in respect of OTC derivatives, can clear those OTC derivatives on that CCP (Article 4 EMIR); ■ ESMA will be obliged to consider whether to impose the clearing obligation on OTC derivatives cleared by the CCP (Article 5 EMIR);	CCP must apply to ESMA for recognition and the following conditions satisfied. European Commission must have adopted an implementing act determining that: ■ The legal and supervisory arrangements of the non-EU state "ensure that CCPs authorised in that ... country comply with legally binding arrangements which are equivalent to the requirements laid down in Title IV [EMIR]"; ■ Those CCPs are subject to "effective supervision and enforcement" in the non-EU state on ongoing basis;	Reciprocity requirement applies. Transitional arrangements exist under EMIR and CRR for existing CCPs that applied for recognition before 15 September 2013 (Article 89(3) and (4) EMIR and Article 497 CRR). The CRR transitional period has been extended to 15 December 2015.

EMIR (continued)

Equivalence assessment	Benefits/consequences	Process and criteria	Comments
Article 25 EMIR provides a procedure for recognising third country CCPs as equivalent (in force) – continued	▪ the CCP will be treated as a QCCP for the purposes of Capital Requirements Regulation (CRR) so that e.g. EU banks and investment firms can benefit from a preferential 2% risk weighting for exposures to the non-EU CCP (Articles 300-311 CRR).	▪ The legal framework in the non-EU state provides for "an effective equivalent system" for the recognition of CCPs authorised under other countries' legal regimes CCP must be authorised in the relevant non-EU state and is subject to effective supervision and enforcement ensuring full compliance with the local prudential framework Cooperation arrangements must have been established between ESMA and the relevant non-EU competent authorities . CCP must be established or authorised in a non-EU state recognised as having systems for anti-money laundering and combating terrorist finance equivalent to EU standards in accordance with criteria set out in the existing common EU understanding on third country equivalence under EU anti-money laundering directive.	CCPs from Australia, Hong Kong, Japan and Singapore have been recognised under Article 25 EMIR. There are pending applications from CCPs in over a dozen countries. The co-operation arrangements with ESMA must provide for: ▪ Prompt exchange of information between them, including access to all information requested by ESMA on CCPs authorised in non-EU states ▪ Prompt notification to ESMA where the non-EU authority deems a CCP supervised by it to be in breach of local requirements ▪ Prompt notification to ESMA where a CCP supervised by it has been granted the right to provide clearing services to clearing members/clients established in the EU ▪ Coordination of supervisory activities, including where appropriate onsite inspection

MiFID2/MiFIR

Equivalence assessment	Benefits/consequences	Process and criteria	Comments
Article 4(1) Prospectus Directive (PD) provides for recognition of third country markets as equivalent to regulated markets (since 31 December 2010).	Where the Commission has assessed a third country regime to be equivalent: ■ EU investment firms may satisfy mandatory on venue trading requirement for shares by concluding transactions on a regulated market authorised in that third country (from 3 January 2017 - Article 23(1) MiFIR). ■ Appropriateness requirements are waived for EU investment firms conducting execution only transactions in certain shares and bonds admitted to trading on a regulated market authorised in that third country (from 3 January 2017 - Article 25(4)(a)(i) and (ii) MiFID2). ■ Securities may be offered to existing and former directors and employees in the EU of a non-EU issuer and its affiliates without a prospectus where the issuer's securities whose securities are admitted to trading on a regulated market authorised in that third country and certain other conditions are satisfied (from transposition of amendments to Article 4(1)(e) PD into national law, required by 1 July 2012).	On the request of the competent authority of a Member State, the Commission shall adopt equivalence decisions stating whether the legal and supervisory framework of a third country ensures that a regulated market authorised in that third country complies with legally binding requirements which are, for the purpose of the application of the exemption under Article 4(1)(e) PD, equivalent to the requirements resulting from: ■ the Market Abuse Directive (2003/6/EC); ■ Title III of MiFID1 (2004/39/EC); ■ the Transparency Obligations Directive (2004/109/EC); ■ and which are subject to effective supervision and enforcement in that third country. The competent authority shall indicate why it considers that the legal and supervisory framework of the third country concerned is to be considered equivalent and shall provide relevant information to this end. The Commission adopts its decision in accordance with the regulatory procedure specified in Articles 5 and 7 of Council Decision 1999/468/EC (Article 25(2) PD).	No reciprocity requirement applies. No determinations have yet been made under Article 4(1) PD. Request has to be made by a national competent authority. A non-EU legal and supervisory framework may be considered equivalent where it fulfils at least the following conditions: ■ the markets are subject to authorisation and to effective supervision and enforcement on an ongoing basis; ■ the markets have clear and transparent rules regarding admission of securities to trading so that such securities are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable; ■ security issuers are subject to periodic and ongoing information requirements ensuring a high level of investor protection; and ■ market transparency and integrity are ensured by the prevention of market abuse in the form of insider dealing and market manipulation. The repeal and replacement of the Market Abuse Directive, MiFID1 and recent amendments to the Transparency Obligations Directive will affect the applicable criteria. The Commission may adopt delegated acts further defining the criteria under Article 4(1) PD (but has not done so).

MiFID2/MiFIR (continued)

Equivalence assessment	Benefits/consequences	Process and criteria	Comments
Article 28(4) MiFIR provides for the recognition of the equivalence of third country regimes with respect to trading venues authorised in those countries (in force, but recognition does not take effect until 3 January 2017).	Where the Commission has determined a third country regime to be equivalent with respect to a category of trading venue: ■ Counterparties may satisfy the mandatory on venue trading requirement for OTC derivatives by execution on a trading venue of that category established in that third country, but only if the third country provides effective reciprocal access for EU venues (from 3 January 2017 – Article 28(1)(d) MiFIR). ■ if the determination covers markets in the third country regarded as a equivalent to regulated markets, derivatives traded on a such a market in that third country are "exchange traded derivatives" (Article 2(1)(32) MiFIR) and are subject to the restrictions on the use of indirect clearing arrangements provided for in Article 30 MiFIR (from 3 January 2017). ■ Trading venues of that category established in the third country may request access to an EU CCP (from 3 January 2017 - Article 38(1) MiFIR).	The Commission may adopt decisions determining that the legal and supervisory framework of a third country ensures that a trading venue authorised in that third country complies with legally binding requirements which are equivalent to the requirements for EU regulated markets, MTFs or OTFs, resulting from MiFID2/MiFIR and the Market Abuse Regulation (596/2014) and which are subject to effective supervision and enforcement in that third country. Decisions shall be for the sole purpose of determining eligibility as a trading venue for derivatives subject to the trading obligation. A decision may be limited to a category or categories of trading venues. The Commission acts in accordance with the examination procedure referred to in Article 51(2) MiFIR.	Reciprocity requirement applies in relation to the trading mandate. There will still be a mismatch between the definition of exchange traded derivatives under MiFIR and the definition of OTC derivatives under EMIR in relation to derivatives executed on non-EU markets. The legal and supervisory framework of a third country is considered to have equivalent effect where that framework fulfils all the following conditions: ■ trading venues in that third country are subject to authorisation and to effective supervision and enforcement on an ongoing basis; ■ trading venues have clear and transparent rules regarding admission of financial instruments to trading so that such financial instruments are capable of being traded in a fair, orderly and efficient manner, and are freely negotiable; ■ issuers of financial instruments are subject to periodic and ongoing information requirements ensuring a high level of investor protection; ■ it ensures market transparency and integrity via rules addressing market abuse in the form of insider dealing and market manipulation.

MiFID2/MiFIR (continued)

Equivalence assessment	Benefits/consequences	Process and criteria	Comments
Article 38(3) MiFIR provides for the recognition of the equivalence of third country regimes regulating trading venues and CCPs (in force, but recognition does not take effect until 3 January 2017).	Trading venues and CCPs established in third countries are only permitted to: ■ make use of the rights of access to EU CCPs and trading venues provided for in Articles 35 and 36 MiFIR if they are established in a third country determined to be equivalent (from 3 January 2017 - Article 38(1) MiFIR); ■ request a licence and the access rights to EU benchmarks provided for in Article 37 MiFIR if they are established in a third country determined to be equivalent (from 3 January 2017 - Article 38(2) MiFIR).	The Commission must have adopted a decision that the legal and supervisory system in the third country provides effective equivalent reciprocal access to local CCPs, trading venues and benchmarks to EU trading venues and CCPs (in the case of benchmarks on a fair, reasonable and non-discriminatory basis). The Commission acts in accordance with the examination procedure referred to in Article 51(2) MiFIR.	Reciprocity requirement applies.

Glossary

- **CCP:** central counterparty
- **Commission:** the European Commission
- **Council:** the Council of the European Union
- **EMIR:** the EU regulation on OTC derivatives, central counterparties and trade repositories
- **ETD:** exchange traded derivatives
- **ESMA:** the European Securities and Markets Authority
- **EU:** European Union
- **MiFID1:** the EU Markets in Financial Instruments Directive
- **MiFID2/MiFIR:** the EU directive and regulation repealing and replacing MiFID1
- **MTF:** multilateral trading facility as defined in MiFID2/MiFIR
- **OJ:** Official Journal
- **OTF:** organised trading facility as defined in MiFID2/MiFIR
- **PD:** Prospectus Directive
- **Parliament:** the European Parliament
- **RTS:** regulatory technical standards proposed by an ESA and adopted by the Commission under powers conferred by an EU regulation or directive
- **SFTR:** the recently agreed Regulation on Securities Financing Transactions
- **Third country:** a state that is not an EU member state

Clifford Chance contacts

Chris Bates
Partner, London
T: +44 20 7006 1041
E: chris.bates
@cliffordchance.com

Marc Benzler
Partner, Frankfurt
T: +49 697199 3304
E: marc.benzler
@cliffordchance.com

Anna Biala
Advocate, Warsaw
T: +48 22429 9692
E: anna.biala
@cliffordchance.com

Lucio Bonavitacola
Partner, Milan
T: +39 028063 4238
E: lucio.bonavitacola
@cliffordchance.com

José Manuel Cuenca
Partner, Madrid
T: +34 91590 7535
E: josemanuel.cuenca
@cliffordchance.com

Lounia Czupper
Partner, Brussels
T: +32 2533 5987
E: lounia.czupper
@cliffordchance.com

Caroline Dawson
Senior Associate, London
T: +44 20 7006 4355
E: caroline.dawson
@cliffordchance.com

Simon Gleeson
Partner, London
T: +44 20 7006 4979
E: simon.gleeson
@cliffordchance.com

Frank Graaf
Partner, Amsterdam
T: +31 20711 9150
E: frank.graaf
@cliffordchance.com

Steve Jacoby
Partner, Luxembourg
T: +352 485050 219
E: steve.jacoby
@cliffordchance.com

Frederic Lacroix
Partner, Paris
T: +33 14405 5241
E: frederick.lacroix
@cliffordchance.com

Caroline Meinertz
Partner, London
T: +44 20 7006 4253
E: caroline.meinertz
@cliffordchance.com

Habib Motani
Partner, London
T: +44 20 7006 1718
E: habib.motani
@cliffordchance.com

Stephanie Peacock
Lawyer, London
T: +44 20 7006 4387
E: stephanie.peacock
@cliffordchance.com

Jeremy Walter
Partner, London
T: +44 20 7006 8892
E: jeremy.walter
@cliffordchance.com

Ute Brunner-Reumann
Counsel, Frankfurt:
T: +49 697199 3234
E: ute.reumann
@cliffordchance.com

Worldwide contact information

36* offices in 26 countries

Abu Dhabi
Clifford Chance
9th Floor, Al Sila Tower
Abu Dhabi Global Market Square
PO Box 26492
Abu Dhabi
United Arab Emirates
Tel +971 (0)2 613 2300
Fax +971 (0)2 613 2400

Amsterdam
Clifford Chance
Droogbak 1A
1013 GE Amsterdam
PO Box 251
1000 AG Amsterdam
The Netherlands
Tel +31 20 7119 000
Fax +31 20 7119 999

Bangkok
Clifford Chance
Sindhorn Building Tower 3
21st Floor
130-132 Wireless Road
Pathumwan
Bangkok 10330
Thailand
Tel +66 2 401 8800
Fax +66 2 401 8801

Barcelona
Clifford Chance
Av. Diagonal 682
08034 Barcelona
Spain
Tel +34 93 344 22 00
Fax +34 93 344 22 22

Beijing
Clifford Chance
33/F, China World Office 1
No. 1 Jianguomenwai Dajie
Chaoyang District
Beijing 100004
China
Tel +86 10 6535 2288
Fax +86 10 6505 9028

Brussels
Clifford Chance
Avenue Louise 65 Box 2
1050 Brussels
Belgium
Tel +32 2 533 5911
Fax +32 2 533 5959

Bucharest
Clifford Chance Badea
Excelsior Center
28-30 Academiei Street
12th Floor, Sector 1
Bucharest, 010016
Romania
Tel +40 21 66 66 100
Fax +40 21 66 66 111

Casablanca
Clifford Chance
169, boulevard Hassan 1er
Casablanca 20000
Morocco
Tel +212 520 132 080
Fax +212 520 132 079

Doha
Clifford Chance
QFC Branch
Suite B, 30th floor
Tornado Tower
Al Funduq Street
West Bay PO Box 32110
Doha
State of Qatar
Tel +974 4491 7040
Fax +974 4491 7050

Dubai
Clifford Chance
Building 6, Level 2
The Gate Precinct
Dubai International Financial Centre
PO Box 9380
Dubai
United Arab Emirates
Tel +971 4 362 0444
Fax +971 4 362 0445

Düsseldorf
Clifford Chance
Königsallee 59
40215 Düsseldorf
Germany
Tel +49 211 43 55-0
Fax +49 211 43 55-5600

Frankfurt
Clifford Chance
Mainzer Landstraße 46
60325 Frankfurt am Main
Germany
Tel +49 69 71 99-01
Fax +49 69 71 99-4000

Hong Kong
Clifford Chance
27th Floor
Jardine House
One Connaught Place
Hong Kong
Tel +852 2825 8888
Fax +852 2825 8800

Istanbul
Clifford Chance
Kanyon Ofis Binasi Kat 10
Büyükdere Cad. No. 185
34394 Levent
Istanbul
Turkey
Tel +90 212 339 0001
Fax +90 212 339 0098

Jakarta**
LWP
DBS Bank Tower
Ciputra World One 28th Floor
Jl. Prof. Dr. Satrio Kav 3-5
Jakarta 12940
Indonesia
Tel +62 21 2988 8300
Fax +62 21 2988 8310

Kyiv
Clifford Chance
75 Zhylyanska Street
01032 Kyiv
Ukraine
Tel +380 44 390 5885
Fax +380 44 390 5886

London
Clifford Chance
10 Upper Bank Street
London, E14 5JJ
United Kingdom
Tel +44 20 7006 1000
Fax +44 20 7006 5555

Luxembourg
Clifford Chance
10 boulevard G.D. Charlotte
B.P. 1147
L-1011 Luxembourg
Grand-Duché de Luxembourg
Tel +352 48 50 50 1
Fax +352 48 13 85

Madrid
Clifford Chance
Paseo de la Castellana 110
28046 Madrid
Spain
Tel +34 91 590 75 00
Fax +34 91 590 75 75

Milan
Clifford Chance
Piazzetta M.Bossi, 3
20121 Milan
Italy
Tel +39 02 806 341
Fax +39 02 806 34200

Moscow
Clifford Chance
Ul. Gasheka 6
125047 Moscow
Russian Federation
Tel +7 495 258 5050
Fax +7 495 258 5051

Munich
Clifford Chance
Theresienstraße 4-6
80333 Munich
Germany
Tel +49 89 216 32-0
Fax +49 89 216 32-8600

New York
Clifford Chance
31 West 52nd Street
New York, NY 10019-6131
USA
Tel +1 212 878 8000
Fax +1 212 878 8375

Paris
Clifford Chance
1 rue d'Astorg
CS 60058
75377 Paris Cedex 08
France
Tel +33 1 44 05 52 52
Fax +33 1 44 05 52 00

Perth
Clifford Chance
Level 7, 190 St Georges Terrace
Perth, WA 6000
Australia
Tel +618 9262 5555
Fax +618 9262 5522

Prague
Clifford Chance
Jungmannova Plaza
Jungmannova 24
110 00 Prague 1
Czech Republic
Tel +420 222 555 222
Fax +420 222 555 000

Riyadh
Clifford Chance
Building 15, The Business Gate
King Khaled International Airport Road
Cordoba District, Riyadh
P.O. Box: 90239, Riyadh 11613,
Kingdom of Saudi Arabia
Tel +966 11 481 9700
Fax +966 11 481 9701

Rome
Clifford Chance
Via Di Villa Sacchetti, 11
00197 Rome
Italy
Tel +39 06 422 911
Fax +39 06 422 91200

São Paulo
Clifford Chance
Rua Funchal 418 15th Floor
04551-060 São Paulo SP
Brazil
Tel +55 11 3019 6000
Fax +55 11 3019 6001

Seoul
Clifford Chance
21st Floor, Ferrum Tower
19, Eulji-ro 5-gil
Jung-gu, Seoul 100-210
Korea
Tel +82 2 6353 8100
Fax +82 2 6353 8101

Shanghai
Clifford Chance
40th Floor
Bund Centre
222 Yan An East Road
Shanghai 200002
China
Tel +86 21 2320 7288
Fax +86 21 2320 7256

Singapore
Clifford Chance
12 Marina Boulevard
25th Floor Tower 3
Marina Bay Financial Centre
Singapore 018982
Tel +65 6410 2200
Fax +65 6410 2288

Sydney
Clifford Chance
Level 16
No. 1 O'Connell Street
Sydney NSW 2000
Australia
Tel +612 8922 8000
Fax +612 8922 8088

Tokyo
Clifford Chance
Akasaka Tameike Tower, 7th Floor
17-7 Akasaka 2-Chome
Minato-ku, Tokyo 107-0052
Japan
Tel +81 3 5561 6600
Fax +81 3 5561 6699

Warsaw
Clifford Chance
Norway House
ul. Lwowska 19
00-660 Warszawa
Poland
Tel +48 22 627 11 77
Fax +48 22 627 14 66

Washington, D.C.
Clifford Chance
2001 K Street NW
Washington, DC 20006 - 1001
USA
Tel +1 202 912 5000
Fax +1 202 912 6000

* Clifford Chance's offices include a second office in London at 4 Coleman Street, London EC2R 5JJ.
** Linda Widyati & Partners in association with Clifford Chance.