



Legal Alert: CFTC and EU Regulators Agree on a Common Approach for the Regulation of CCPs

February 12, 2016

Earlier this week, the Commodity Futures Trading Commission (CFTC) and European regulators announced that they have reached agreement on a “common approach” regarding requirements for central counterparties (CCPs) (i.e., clearinghouses). Per their [joint statement](#), the European Commission will, in the very near term, adopt an equivalence determination with respect to CFTC requirements for U.S. CCPs that will allow the European Securities and Markets Authority (ESMA) to “recognize” U.S. CCPs.

Why is this relevant?

Under the European Union’s (the EU) [Capital Requirements Regulation](#), EU banks and their subsidiaries incur higher capital charges if they use a CCP that is not a “qualifying” CCP (a QCCP), i.e., a CCP that is not recognized or authorized by ESMA. These capital requirements are not currently effective; they have been delayed multiple times due to the failure on the part of the CFTC and European regulators to reach agreement to recognize each other’s CCP regulatory regimes as equivalent. The current compliance date for these capital requirements is June 15, 2016.

According to the CFTC’s and EU’s joint statement, the European Commission will propose its equivalence determination with respect to U.S. CCPs as soon as practicable, after which it will be voted on by the Member States of the European Union. Following this step, ESMA may complete the process for recognizing U.S. CCPs.

The CFTC’s and EU’s agreement comes just in time. The first deadline for the clearing of interest rate swaps under EU regulations is June 21, 2016,ⁱ and the frontloading window applicable to those market participants that are subject to the June 21 deadline opens on February 21, 2016.ⁱⁱ In light of this deadline, EU banks were expected to cease using U.S. CCPs in advance of the February 21, 2016, date in order to avoid the capital requirements.

The joint statement indicates that U.S. CCPs are expected to be recognized by ESMA by the June 21 clearing compliance date, and states that EU banks can continue to use U.S. CCPs during ESMA’s recognition process. This permits EU banks to use US CCPs to satisfy the EU clearing requirements. In turn, the joint statement indicates that the CFTC will “propose a determination of comparability with respect to EU requirements, which will permit EU CCPs to provide services to US clearing members and clients whilst complying with certain corresponding EU requirements.” The CFTC will also propose to streamline the registration process for EU CCPs wishing to register as derivatives clearing organizations in the United States.

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What's next?

The CFTC's and European regulators' actions to deem EU CCP requirements equivalent to U.S. CCP requirements do not fully solve the equivalence issue with respect to mandatory clearing. While it will now be possible to satisfy the clearing requirement of either jurisdiction by using an EU or U.S. CCP, the clearing requirements for particular products have not yet been deemed comparable. Thus, substituted compliance, which would permit compliance with one jurisdiction's clearing requirement (or non-clearing requirement) to satisfy the other's, is not yet available. This is not of major concern, because the EU's clearing requirement for interest rate swaps, which is the only mandatory clearing determination that has been finalized in the EU thus far, is nearly the same as the U.S. clearing requirement for interest rate swaps.ⁱⁱⁱ

The joint statement indicates that U.S. and EU regulators will continue to work together to harmonize all of their jurisdictions' respective requirements for swaps.

ⁱ See Sutherland's September 1, 2015 Legal Alert, "[Coming Soon: Mandatory Clearing of Interest Rate Swaps Under EMIR](#)," for more information about the EU's clearing requirement for interest rate swaps. Note that the compliance dates for the EU's interest rate swaps clearing requirement are as follows:

Category 1	Counterparties that are clearing members of CCPs that are either authorized or recognized for the purpose of the clearing organization.	June 21, 2016
Category 2	"Financial Counterparties" (FCs), and alternative investment funds (AIFs) or collective investments in transferable securities that are "Non-Financial Counterparties" that exceed certain specified clearing thresholds (NFC+s), which are not in Category 1 and whose aggregate month-end average notional amount of non-centrally cleared derivatives is above EUR 8 billion for the three months following publication of the regulatory technical standards for interest rate swaps clearing in the Official Journal of the European Union (excluding the month of publication).	Dec. 21, 2016
Category 3	FCs and AIFs that are NFC+s below the EUR 8 billion threshold which are not in Category 1 or Category 2.	June 21, 2017
Category 4	NFC+s not included in Categories 1-3.	Dec. 21, 2018

Also note that, by virtue of remaining maturities established in the EU's final regulatory technical standards for clearing, frontloading will only apply to Category 1 and 2 entities, and the frontloading period begins on February 21, 2016, and May 21, 2016, respectively.

ⁱⁱ While a misnomer, "frontloading" refers to retroactive clearing.

ⁱⁱⁱ The classes of interest rate swaps required to be cleared in the EU are similar but not identical to those required to be cleared in the U.S. The differences between the clearing mandates include the following: (i) the U.S. rules require the clearing of forward rate agreements denominated in JPY but the EU rules do not and (ii) the maximum maturity for the overnight index swap class is two years under U.S. rules and three years under the EU rules.

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