

Regulatory Update

CCPs in focus. And Oversight itself.

As well as all the usual focus on the latest regulatory developments, this is an Oversight with a difference.

The European Union finally has a new – and finalised – Regulation on “OTC derivatives, central counterparties and trade repositories”, that’s EMIR to you and me. Since SIX x-clear Ltd is such a key part of our strategy, we thought it would be a good idea to turn the spotlight on the new regulatory framework as this affects CCPs. And with it, some initial thoughts on how these new rules might impact you, our clients and customers. So this is the main feature this quarter.

But we haven’t neglected other aspects: there is the rather more prosaic passage of the CSD Regulation through the Brussels legislative cycle with the enhancement of one particularly negative aspect of the proposal to which we have previously alerted you.

Although CPSS-IOSCO have finalized their Principles for Financial Market Infrastructures, they have been no less busy by publishing a further consultation on the “Resolution and Recovery Framework for FMIs”.

Finally, this is the eighth edition of Oversight, and as we have been running it for nearly two years, we thought it would be a good time to take stock. We know that you welcome Oversight but there is always room for improvement. We would greatly appreciate it if you could take the time to complete a very short survey.

There are no prizes for the fastest submitted form but the result could be a much improved Oversight.

Thomas Zeeb
CEO
SIX Securities Services

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Oversight
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Welcome to Oversight - our quarterly update on market policy developments and the regulatory landscape. If you would like to subscribe to this newsletter electronically please send an e-mail to oversight@six-group.com

If you would like to learn more about topics covered in this edition, please contact: Alex Merriman, Head of Market Policy (alexander.merriman@six-group.com) or at +41 58 399 4583.



EU Initiatives affecting the value chain

Negotiations on the CSD Regulation have begun slowly, and we focus extensively on EMIR, and draft Technical Standards issued by ESM, EBA and the Joint ESA Committee, as well as Banking Union.

EU Legislative Programme affecting Market Infrastructures

Changes since the last edition of Oversight are highlighted in bold in the table below:

Segment of the Value Chain	Measure	Proposed (Published)	Adopted (Finalised)	Entry into Force (after Technical Standards)
Trading	Review of MiFIDII/MiFIR	20 October 2011	End - 2012 ?	2015
Clearing	EMIR	15 September 2010	July 2012	End - 2012
Settlement	RCSD	7 March 2012	Mid - 2013 ?	Mid - 2015
Underpinning Law	Securities Law Directive (SLD)	Q4 2012 / Q1 2013	End - 2015 ?	2017 / 18?

Central Securities Depositories Regulation (CSDR)

The dossier was handed over to the Cyprus Presidency on 1 July and a Council Working Group (CWG) discussion took place on 18 July. Progress remains slow; this last meeting reviewed the text handed over by the Danish Presidency, and our understanding is that the Council have yet to broach some of the more difficult issues, such as the treatment (legal separation) of CSDs' banking-type services. The next CWG takes place on 21 September; but because the European Parliament has postponed its vote on MiFID2/MiFIR, and the Presidency has to tackle other priorities such as the crisis management framework for banks, we suspect that the RCSD will continue to rank as a low priority. Meanwhile the EP's ECON committee released its draft report on the CSDR. This was something of a disappointment for the CSD community, as the Rapporteur, Kay Swinburne, supported the Commission's line on separating CSDs' banking-type services and, moreover, proposed the deletion of a derogation that would have permitted national authorities to allow its CSD a "1 + 2" model. This continues to be European CSDs' preference, so that we will, through our Trade Association, ECSDA, be following this closely. The EP report will be subject to discussion in ECON in September, followed by the tabling and adoption of amendments in mid-October. The report could be further adopted by the EP Plenary

Session before Christmas. Thereafter, depending on the state of discussions in the Council, it is expected that a Trialogue will be convened in the early months of 2013, and will require the following Irish Presidency to finalise the dossier.

Feature: New EU and Global Rules impacting on CCPs (including EMIR)

The Text of EMIR has been finalised and was published in the EU's Official Journal on 27 July. Because Regulations take direct effect in the European legal nomenclature, EMIR took legal effect on 16 August. To recollect, EMIR implements the EU's adoption of the G-20 commitment for the trading, central clearing and reporting of OTC derivatives, as well as instituting an EU supervisory regime for Trade Repositories. The part which particularly affects CCPs in Europe, including SIX x-clear relates to new authorisation, supervision and ongoing governance and risk management requirements. One particular effect will require all CCPs in Europe to seek re-authorisation by the European Securities Authority, ESMA, by the end of June 2013.

EMIR should be broadly read in conjunction with the aspects relating to CCPs from the CPSS-IOSCO Principles for Financial Market Infrastructures (PFMI). However, the requirements in EMIR are gener-



ally speaking more onerous. CCPs in the EU will be required to maintain minimum capital of at least €7.5mn, as well as additional dedicated financial resources against the failure of a clearing member (beyond dipping into the resources provided by the default waterfall). As previously mentioned, facilities will need to be put in place to offer clearing members a choice of “global omnibus” or segregated client accounts. Governance requirements are also being tightened up: CCPs will require clearly documented risk management and other procedural requirements; a separate Board, with sufficient non-independent Directors, as well as a dedicated CRO, CFOs and CAO.

A number of aspects of EMIR are being clarified by Technical Standards (TS) being developed by ESMA, the European Banking Authority, and the Joint Committee of all three ESAs. For the most part these draft TS will have to be submitted to the European Commission by the end of September. However, the submission of those being prepared by the Joint Committee on the capital treatment of non-centrally cleared OTC derivatives has been postponed until a later date. This is to ensure that the EU does not jump ahead of the current parallel consultation being undertaken by the Basel Committee (BCBS) and IOSCO. BCBS-IOSCO have also recently finalised their advice on the treatment of bank exposures to CCPs, which will also be reflected in a complementary EBA TS, on banks’ exposures to both margins (weighted at 2%) and the default fund (weighted at something in excess of 2%). Finally, ESMA is clarifying a range of regulatory treatments proposed in EMIR. For instance, (referred to above) in the extent of additional CCP financial resources, and how this is measured (against total capital), the parameters of stress-testing (through a range of indicators) and required confidence intervals for the failure of clearing members, to name just three.

Internally, x-clear has begun the process of comparing the impact of EMIR (and the revised CPSS-IOSCO Principles for Financial Market Infrastructures) on current processes, with a view to ensuring that it is compliant with the revised requirements by the time of its submitting its application to ESMA for re-authorisation by the middle of 2013. We will also be putting in place an internal “regulatory” project, which will start with EMIR and other CCP requirements, but also embrace other initiatives such as CSDR and T2S, in determining the longer-term impact on the whole of Division Securities Services, including and x-clear and SIS.

Revision of the Market in the Financial Instruments Directive (MiFID II/MiFIR)

As mentioned above, the European Parliament has deferred its vote on the Commission proposals until

the post-summer holiday resumption in September. This is so as to enable a consensus to emerge on a number of still unresolved issues: the treatment of high frequency trading and the new category of trading venue, the OTF, the controversial Third Country aspects, as well as the choice of, and access to, clearing venues offered by trading venues. The Cyprus Presidency has made this dossier a priority and is still intending to obtain agreement in the Council by the end of this year.

Commission Proposals on inclusion of benchmarks in revised market abuse and insider dealing regimes

On 25 July, the European Commission published its proposals in relation to the above to prohibit the manipulation of benchmarks and to make such manipulation a criminal offence. While largely a consequence of, and a response to, the recently-revealed manipulation of interest rate benchmarks, such as LIBOR and EURIBOR, the wide scope of the definition, means that equity-based indices such as the FTSE 100, Euro-Stoxx and the SMI could also be caught. Via its trade association FESE, securities exchanges, such as the SIX Swiss Exchange, can be expected to oppose this generalised catch all.

Banking Union

As part of its response to dealing with the euro-zone crisis, the European Commission is examining ways of further integrating certain key aspects of the EU regulatory and supervisory regime, and is expected to come up with firm proposals in September. As widely trailed, these could include mutualising deposit guarantee schemes, establishing a common pan-European bank resolution fund and, particularly centralising supervision of EU banks in a single body, such as the ECB. This could call into question the current, finely-balanced, division of competences and responsibilities between Member States’ national authorities, on the one hand, and the European Supervisory Authorities, particularly the EBA, on the other. It does not require a great leap of imagination to envisage that such a further centralisation of supervision in a single body could also, because of their systemic importance, eventually embrace EU FMIs.

If you would like to find out more on EU market infrastructure legislation or on any other topic, please contact: Alex Merriman, Head of Market Policy (Alexander.Merriman@six-group.com or 058 399 4583). Previous editions of Oversight and other regulatory information about us are also available at: www.six-securities-services.com.

Market infrastructure initiatives by the European Central Bank (ECB)

24 CSDs have signed up to the T2S project, while a decision on SIS's connectivity solution has still to be determined.



Target 2 Securities (T2S)

As widely anticipated, no fewer than 24 European CSDs, including SIX SIS have now signed the Framework Agreement with the ECB, by the deadline of the end of June. With the next phase of the project underway, the ECB Guideline from 2010 dealing with the aims, objectives and governance of the project has been amended. This was published in the Official Journal on 11 August. As before the Governing Council of the ECB is the ultimately decision making body, and will be assisted by the T2S Board and the

4CB, with a re-cast Advisory Group and CSD Steering Group. The Guideline of 18 July also includes a definition of a "CSD" and the access criteria to T2S for CSDs, both which have read across to the CSDR. Following the SIX Group Board meeting on 18 June, which approved SIS's connection to T2S, SIS is now examining in more detail the manner of the connection, including the associated financial projections. This will be reviewed by the SIX Group Board in December, for a final decision.

Other legislative and regulatory initiatives impacting market infrastructures and the value chain

Resolution is very much the focus this Quarter's with a new consultation from CPSS-IOSCO on recovery and resolution plans for FMI's, as well as the United Kingdom's proposals to extend the UK resolution regime for banks (under the Banking Act 2009) to other key institutions such as FMI's.

CPSS-IOSCO Consultation on recovery and resolution for Financial Market Infrastructure

Following the finalisation of its Principles in April, and the launch of two consultations, covering the underpinning Assessment Methodology and a Disclosure Framework, CPSS-IOSCO launched a further consultation on 29 July on recovery and resolution plans for FMI's. This follows parallel "key attributes" initiative for Globally-systemically important financial institutions ("G-SIFIs") and Domestic-SIFIs launched by the Financial Stability Board and the Basel Committee. The Consultation, which closes on 28 September, similarly proposes that all FMI's should formulate Recovery and Resolution Plans ("RRPs"), and that national authorities should be endowed with the necessary toolkit to deal with failing FMI's. The proposal is, to a large extent, focussed on CCPs, but some aspects also apply to CSDs. "Recovery" refers to processes and procedures which FMI's can deploy in the event of the failure of one or more of their participant(s). For a CCP, this is typically the default waterfall, where the margin and default fund contributions of the failing participant are used to mitigate the losses arising from the failure. "Resolution" is about the tools which a national authority can deploy, for instance the further

mutualisation of losses, further equity offsets or a stay or termination rights.

UK Consultation on broadening the financial sector resolution regime

Via the Banking Act 2009, the UK already has a recovery and resolution regime for banks and, in a consultation dated 1 August, is proposing to extending the regime to other institutions including CCPs and other FMI's. Essentially, the extension will give the same powers to the Bank of England over FMI's, as it already enjoys over banks, notably in directing a institution towards a solution, replacing its management, and in winding it down. The UK judges it necessary to introduce these powers as soon as possible, as progress in the EU for comparable powers is slow. The consultation closes on 24 September.

If you would like to find out more on any of these topics, please contact: Alex Merriman, Head of Market Policy (Alexander.Merriman@six-group.com or +41 58 399 4583). Previous editions of Oversight and other regulatory information related to us are also available at: www.six-securities-services.com.

Survey

Oversight has now appeared for eight editions in nearly two years and SIX Securities Services would appreciate it if you could complete the short survey below. Please scan and e-mail your results to oversight@six-securities-services.com. Thank you.

How would you rate the following?

	Excellent	Very Good	Good	Average	Poor
Editorial	<input type="checkbox"/>				
EU developments	<input type="checkbox"/>				
Non-EU developments	<input type="checkbox"/>				

What do you think are the best features of Oversight?

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What would you like to see more of?

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What do you think are the less positive features of Oversight?

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What would you like to see less of?

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Is the frequency - quarterly - about right?

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Any other comments that you have...

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