

clear to trade



Eurex Clearing AG

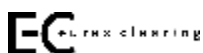
Response

CESR Call for Evidence

Formal request for technical advice on identification of regulatory arrangements for post-trading infrastructures and to advise on possible solutions in terms of bridging any potential differences in these arrangements

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A. Introduction

The Committee of European Securities Regulators (CESR) has requested by 19th September, technical advice on identification of regulatory arrangements for post-trading infrastructures and to advise on possible solutions in terms of bridging any potential differences in these arrangements. This call for evidence follows a request from the European Commission following up on the initiative conducted by CESR's Post-Trading Expert Group (PTEG) in late 2007 and early 2008 to map regulatory arrangements currently in place in all jurisdictions. The PTEG initiative has been established in the context of the large and growing number of requests (presently more than 80) for access and interoperability among trading platforms, CCPs, and CSDs taking place under the Access and Interoperability Guideline of the European Code of Conduct for Clearing and Settlement for cash equities.

Eurex Clearing (ECAG)—one of the world's leading clearing organizations providing a complete set of clearing and risk management services for leading exchanges and market places—has been committed to the success of the Code of Conduct since its inception in November 2006. ECAG believes that the Code remains an important step towards the creation of an efficient market environment for cross-border trading in Europe.

ECAG has remained closely engaged throughout the implementation of the Code and in particular has been and continues to be very active in the process of establishing links with other market infrastructure players under the Access and Interoperability Guideline. ECAG has launched requests to enter the Euronext, the SWISS and the UK markets. Through this process, ECAG has gained insight into regulatory and other barriers in various EU jurisdictions. The opportunity to participate in this call for evidence is therefore welcomed, both in terms of ensuring the success of the Code of Conduct as well as in facilitating the development of links to benefit European investors.

B. Comments

Overview of regulatory requirements and processes regarding clearinghouses/CCP.

Regulatory Framework differs by country thereby making the process of establishing a CCP in further countries relatively complex and time consuming

The approval of CCPs requesting access in the different markets is subject to the single national supervisory authorities; this intuitively gives rise to different legal frameworks which again is reflected in how CCP business is regulated; meaning as a “EU non harmonized financial service provider “.

Regulations with respect to operate a clearing house in the **United Kingdom** are currently not stipulated in a legislative form, but are referenced to in connection with the administrative standards published by the FSA. This regulatory framework is comparable to the terms for banks, financial institutions and service providers.

Comparatively, **French regulation** offers on the legislative level some basic rules for the regulatory classification of clearing houses. These rules are interpreted and completed through administrative provisions. Like the UK market, the regulatory framework for CCPs in France is based on the regulations for banks and financial service providers.

By contrast, the **Dutch** market is in the process of finalizing an independent regulatory framework for the activities of a CCP, which will be similarly reflected in national legislation. Seeing as this framework is “work in progress” an assessment of these specific requirements is currently not possible. The supervision of a CCP in the Netherlands is currently based on the supervisory competence with respect to the relevant stock market and is managed by an Annex competence of the Exchange Supervisor. During this transitional period the Dutch National Supervisory Authorities are assessing clearing houses on the basis of the CPSS-IOSCO recommendations for CCPs (11/2004). Likewise the assessment is strongly reliant on the agreement to exchange information with the CCPs National Regulatory Authority, in case of Eurex Clearing this would be the BaFin and its relevant standards.

From the Dutch regulatory perspective as well as the current interpretation of the code there is no link between clearing of different Euronext markets, so that prudentially no linkage is seen in the regulatory approval of a CCP. This suggests that for each market an independent request per market needs to take place, increasing not only the complexity and duration of entry but similarly making it economically unviable.

Further, the assessment of the **Dutch** and **French** market entry was difficult to achieve since there is limited public information available for both the regulatory approval processes for a CCP as well as for general requirements for CCPs.

In the **Swiss market** clearing houses are seen as an important and relevant part of the capital markets fabric. Importance and relevance is hereby dependant on the transactional/order volume processed and the number of clearing members with Swiss origin. These clearing houses are accordingly supervised by the SNB. There are numerous requirements to be met, which in part are similar to the requirements set for banking regulation. In the case where CCPs are already actively supervised by national regulatory authorities, Swiss law does grant the Swiss regulator to waive certain or all regulatory requirements laid down by Swiss law, thereby relying in part or in full on the home regulator and the cooperation between regulatory bodies.

Admission process is often complex and reduces flexibility for the incoming CCP

As a **CCP in France** it is required to have a quasi-banking status. This suggests -in accordance with the provided requirement catalogue- an extensive documentation is to be created and handed in for evaluation to the French regulator. Therefore, a longer approval procedure is foreseen (estimated 6-12 months from the filing of the initial documentation). A "pass porting" of CCP banking permission granted to ECAG under the German Banking Act (KWG) was not considered by the regulator. Furthermore the possibility for a renunciation of a regulation by the French supervisory authorities, as i.e. stipulated in Section 2, Paragraph 4 KWG in the case of an equivalent home state regulation, is not given.

According to current regulatory obligations as well as the need for independent regulation of ECAG for the **Euronext Paris market**, it is likely that future changes in clearing conditions have to be approved by the French supervisory authorities within a month's period. Whether this will be limited to such parts of the clearing conditions which relate to the Euronext Paris market is currently not clear. An additional administrative procedure would reduce the flexibility of the CCP to improve its services for new products or to align itself rapidly to new market conditions.

Furthermore the recommendation is that all Euronext markets need to be simultaneously cleared to secure that the efficiency of clearing across the markets is not reduced or impaired. This would potentially cause mutual interdependencies between the supervisory bodies and likewise impact the timelines to establish a link to each Euronext market.

Due to past activities related to the **UK** legal and market space. ECAG has already achieved the status of "Recognized Overseas Clearing House (ROCH)" at the beginning of 2007. A "pass-porting" of the in Germany granted banking licence was not possible. Similarly, no renunciation of supervision by the foreign regulator, in this case the FSA was considered. The duration of the regulatory recognition process post submission of the initial documents was between 12 and 14 months. This procedure included consultation with other authorities as well as a public consultation.

With respect to the **Swiss market** there will not be a need for a separate permission from the Swiss regulators with regard to the German banking licence of ECAG. Supervision with respect to activities in the Swiss market will be mainly handled on the exchange of information basis with the German regulator BaFin.

Tax regulation act as barriers to CCPs and its members

The transfer of withholding tax affects all relevant markets. Hence ECAG gained experience to handle tax implications, for example on the UK market.

UK Stamp Duty Reserve Tax (SDRT) legislation is based on a SDRT charge arising each time there is a contractual change in beneficial ownership of shares as a result of an agreement to transfer securities.

The HMRC has given exemptions in respect of transactions presented to a CCP by an exchange, the Clearing Relief (eligible for clearing member or its nominee to the CCP) and the Intermediary Relief (non-clearing participant or client to a clearing participant or its nominee).

Nevertheless, SDRT has significant member impact in the course of realizing a link to the UK market. Even if a member has received Intermediary Relief this requires separate

reporting to HM Revenue and Customs. As this would require a new interface for each member as well as at least one settlement account, the only choice is to use the incumbent market infrastructure player for this service.

Reporting requirements may hamper competitive services

Also the registration process for the respective securities has been identified as a further barrier for providing an efficient solution in several markets, i.e. the Spanish market. All stocks in Spanish instruments are subject to a registration. Registered Shares are required as matching criteria at each transfer at the local CSD.

Shares are additionally specified with a register reference indicating trade date and trading location. This reference is applied after each trade and has to be provided to the CSD when the shares are sold next time in order to prevent short selling. Settlement via the CSD requires a local custodian because German institutes are not allowed to keep an account at the CSD leading to higher complexity and costs.

C. Conclusion

As outlined above, ECAG has identified and experienced regulatory differences in several countries for the development of links, especially in regard to CCP links. However all comments are based on best available market knowledge of the analyzed markets, thereby ECAG has also engaged specialized external parties to investigate market, legal and taxation requirements. This does not suggest that there is no room for misinterpretations or misunderstandings, but does imply best current and objective market knowledge attainable. Particularly the different requirements of admission and the duration of the said procedure in each country lead to little or no planning guarantee. This on the other hand imposes unforeseeable (high) costs for allocating resources to meet the requirements in each specific market, with insecure or indeterminable results, as realization of links are dependant on the willingness and ability of third parties to engage.

The regulatory barriers listed and lack of a “level regulatory playing field” lead to the result that the costs and effort to create clearing services under various European regulation do not stand in any relation to the potential gains achievable. So it is no surprise that new CCPs occur cheaper and quicker under one single national regulation as a CCP with a pan-European connection to settlement services.

Against the background of the already mentioned arguments, providing a “passporting” which is intuitively linked with demanding requirements securing both a high level of safety and risk avoidance seems to be the most favourable option. The alternative is the realization of a homogenous and consistent European regulation for CCPs.

As ECAG is keen to see its various link requests go live, it is encouraged by CESR’s call for evidence and remains optimistic that the call will lead to tangible results in the near future.