



European Securities and
Markets Authority

Final Report

**Draft regulatory technical standards on indirect clearing arrangements
under EMIR and MiFIR**

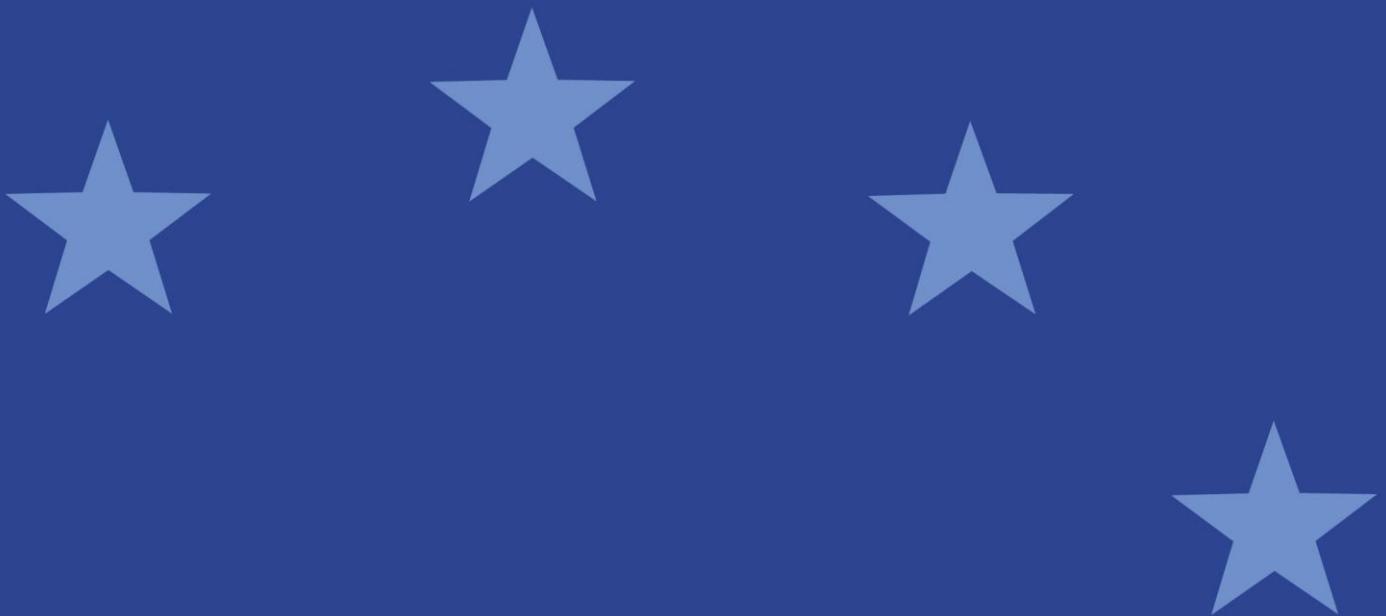


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Acronyms used

CCP	Central Counterparty
EMIR	European Market Infrastructure Regulation – Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
ETD	Exchange-traded derivatives
MiFIR	Markets in Financial Instruments Regulation – Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012
OTC	Over-the-counter
Q&A on EMIR	Questions and Answers on the implementation of EMIR available on ESMA's website
RTS	Regulatory Technical Standards
EMIR RTS	Commission Delegated Regulation (EU) No 149/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on indirect clearing arrangements, the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP

1 Executive Summary

Reasons for publication

Regulation (EU) No 600/2014 (MiFIR) requires ESMA to develop a series of regulatory technical standards (RTS), including RTS on indirect clearing arrangements. These arrangements relate to indirect clearing services for exchange-traded derivatives (ETD).

In addition, ESMA can initiate the review of RTS it has developed to ensure they fulfil their objective and ESMA has been conducting such a review for the RTS on indirect clearing arrangements under Regulation (EU) No 648/2012 (EMIR). These arrangements relate to indirect clearing services for OTC derivatives. The applicable requirements are set in Commission Delegated Regulation (EU) No 149/2013 (EMIR RTS).

The package of the two RTS subject to this report was consulted upon in a consultation paper published in November 2015. The consultation paper focused solely on indirect clearing and covered in the same paper the considerations related to the EMIR RTS, the considerations related to the MiFIR RTS and the consistency between the two. Prior to that consultation the MiFIR RTS had been consulted on as part of the MiFID II/MiFIR consultation in the discussion paper published in May 2014 and in the consultation paper published in December 2014.

With this report, ESMA publishes its final proposals for a) a draft RTS amending the EMIR RTS in order to ensure the EMIR RTS fulfils its objective and b) a draft RTS under the MiFIR mandate (MiFIR RTS) that is consistent with the amended EMIR RTS.

Contents

The report focuses exclusively on indirect clearing arrangements under EMIR and MiFIR, and with respect to the EMIR RTS it does not cover the other items included in the EMIR RTS¹. The report presents the comments received from respondents to the consultation as well as the rationale for the decisions that have been made on whether and how to introduce some changes to the draft RTS that ESMA consulted on.

Annexed to this final report are the legislative mandates related to the two draft RTS (Annex I), the ESMA cost-benefit-analysis (Annex II), and the draft RTS (Annex III).

Next Steps

The final report has been submitted to the European Commission on 26 May 2016. The Commission has three months to decide whether to endorse the technical standards.

¹ The EMIR RTS is also related to the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP.

2 Indirect clearing arrangements

1. Following the publication of the consultation paper ESMA/2015/1628 on 5 November 2015², the 24 responses from stakeholders were analysed and their comments on the draft RTS under EMIR and the draft RTS under MiFIR were taken into account as detailed in the following sections.

2.1 Consistency between the two RTS

2. The consultation paper developed further the rationale for consulting at the same time on both the MiFIR requirements and amendments to the EMIR requirements, as had been communicated to the European Commission in a letter³ sent by ESMA on 2 October 2015. The consultation paper explained the need to review, and in fact amend, the EMIR RTS to ensure it fulfils the objective of the EMIR mandate, and to consider the amendments to the EMIR RTS in conjunction with the draft MiFIR RTS to ensure the consistency mandate between the two RTS is also fulfilled.
3. A majority of respondents did not raise any major concerns with this approach, in fact, some commented on welcoming making changes to the EMIR RTS in order to address the issues participants have faced to develop indirect clearing arrangements for OTC derivatives.
4. However, some respondents commented on some of the nuanced differences that can exist between the OTC derivative market and the ETD market as potentially justifying differentiations between the two RTS. The two main aspects relate to the choice of accounts and the clearing obligation. The choice of accounts is discussed further down in section 2.3 of the final report and the aspect related to the clearing obligation is discussed in section 2.2 of the final report. But overall, in spite of these nuances, the consistency objective can be ensured.

2.2 General comments

5. The consultation paper included a series of questions on the main technical points being addressed via the changes presented in the two draft RTS. However, a few additional points of a more general nature were commented on in the responses. They relate to the territorial scope of the RTS, the access to clearing and the responsibilities of the various participants in managing the risk of indirect clearing arrangements.

Territorial scope

6. Several respondents argued that the RTS needed to include a set of parameters to limit its application to EU entities to the extent possible. In fact some argued that it

² The consultation paper ESMA/2015/1628 and the related responses are available at the following address: <https://www.esma.europa.eu/press-news/consultations/consultation-indirect-clearing-under-emir-and-mifir>

³ The letter (ESMA/2015/1498) sent by ESMA to the European Commission on 2 October 2015 is available at the following address: <http://www.esma.europa.eu/content/Letter-European-Commission-re-RTS-indirect-clearing-under-EMIR-and-under-MiFIR>

should be limited to indirect clearing arrangements where all the entities in the clearing chain are EU entities.

7. ESMA understands that the potential difficulties linked to having one or more third country entities in the clearing chain are compounded with indirect clearing arrangements compared to client clearing arrangements, due precisely to the increased complexity and increased number of layers in indirect clearing arrangements. However, the territorial scope is defined in level 1 legislation; ESMA does not have the mandate to redefine the territorial scope of application of the requirements for indirect clearing services for OTC derivatives and for ETD in the RTS themselves.
8. However, at the same time, ESMA is mindful of the fact that many indirect clearing arrangements include non-EU entities and takes it into account in setting the requirements in the draft RTS. The primary example is the problem discussed in the consultation paper about the potential conflict of law with the applicable insolvency regime when the relevant entity is established in a third country jurisdiction. As stated in the consultation paper, the EU legal framework cannot override the third country insolvency regime. This has led to the drafting of requirements that take this aspect into account as detailed further in the consultation paper in section 2.4 of the final report.
9. In addition, it is important to note that for cross border issues, EMIR relies on a system of equivalence decisions, combined with recognition decisions as far as CCPs are concerned. In this case, EMIR does not require the third country CCP to comply with the EMIR requirements for CCPs but instead relies on the CCPs to be fully compliant with their local regime and be effectively supervised domestically when the applicable CCP regime has been deemed equivalent⁴.
10. As a result, when a jurisdiction is assessed as having equivalent requirements to EMIR for CCPs, then the recognised third country CCPs would not need to comply with the requirements on indirect clearing of the RTS presented in the final report. Specifically, this means that recognised third country CCPs would not necessarily offer the same segregation options as the ones required under EU regulation for indirect clearing. Thus, EU clearing members of these recognised third country CCPs would face a similar situation as the one they face for client clearing with these third country CCPs. This is addressed in ESMA Q&A CCP question 8(j).
11. Finally, some respondents commented on the need for a clarification on who is responsible to ensure other links in the chain are compliant with the RTS, especially when there are non-EU entities in the chain. However, it is not for these draft RTS to specify supervisory responsibilities on third country entities. As with other EU rules, the applicable EU requirements for the provision of financial services within the European Union apply and therefore these RTS will apply to third country entities when they provide services to EU entities.

Access to clearing

⁴ Please refer to Article 25 of EMIR for the exact conditions to be met in order for a third-country CCP to be recognised.

12. Several respondents have commented on the level of access to clearing in relation to these RTS. Broadly speaking, with regard to OTC derivatives, several respondents commented on the importance of setting requirements that can better support the offering of indirect clearing services, in order to facilitate access to clearing when direct membership or becoming a direct client of a clearing member is not possible, not economically viable or not available.
13. With regard to ETD, several respondents flagged that a large part of the market is currently relying on indirect clearing. As a result, the requirements need to take this into account in order not to impact access to some ETD markets for many entities, i.e. not to reduce the access or even shut out certain entities from these ETD markets.
14. ESMA has been paying detailed attention, and is continuing to do so, to the level of access to clearing for both OTC derivatives and ETD in the context of the clearing obligation as well as the EMIR and MiFIR mandates to establish the requirements for indirect clearing arrangements for OTC derivatives and ETD. Indeed, access to clearing means the ability to access trading of the relevant trades. In particular, this aspect of the level of access to clearing has been one key reason for conducting the combined consultation under both the EMIR and the MiFIR mandates.
15. First of all, it has allowed reviewing and assessing what could be done differently to better support the development and the offering of indirect clearing services for OTC derivatives in the context of the EMIR RTS. Secondly, it has also allowed having an additional round of input from stakeholders on the draft MiFIR RTS in the process of its finalisation, in order to better inform the drafting of the requirements.
16. In parallel to the development of these RTS, ESMA will continue to keep an important focus on access to clearing, in particular to ensure a successful implementation of the clearing obligation in the case of OTC derivatives.
17. However, this aspect of access to clearing has also been taken into account when deciding on which changes to make for these RTS. This is for instance reflected in the obligation for clearing members prepared to offer indirect clearing to permit all their clients meeting certain conditions to provide indirect clearing services as detailed in Article 2(1) of the RTS.
18. Several representatives of clearing members argued in their responses that clearing members should have flexibility on which of their direct clients can provide indirect clearing services.
19. Clearing members already have some flexibility in setting criteria to decide on which clients they offer access to clearing. The draft RTS has been modified to clarify that their set of criteria can also contain additional criteria for clients that want to provide indirect clearing services. Recognising the additional risk and complexity associated with indirect clearing, and in line with EMIR Article 37.3, clearing members should be permitted to request that their clients offering indirect clearing have additional resources and operational capacity to perform this activity.
20. However, these criteria need to apply to all clients in a non-discriminatory manner. This means that all the clients meeting these additional criteria should be allowed to provide indirect clearing services. There is no need to introduce additional discrimination between clients as that would not work in favour of wider access to clearing.

21. Finally, some respondents, typically representatives of counterparties that face difficulties finding clearing services, have commented on the potential impact of the leverage ratio on the clearing activity of clearing brokers.
22. The framework for the leverage ratio is still being discussed, including the treatment of client margin and the potential minimum levels. However, some respondents raise the concerns that in anticipation of how the framework may be finalised, some decisions are already being made accordingly by clearing brokers in terms of balance sheet allocation for their clearing activities, thus potentially limiting the amount of access to clearing they are willing to intermediate.
23. As a result, these respondents argue that the clearing offers available to them would still be limited even if all the other concerns raised in the consultation on the indirect clearing requirements were addressed. In light of these difficulties to find clearing services, they commented on the need for an exemption from the clearing obligation for small financial counterparties trading derivatives only for hedging purposes.
24. These elements are related to level 1 considerations which are still in progress or under review, for instance the framework for the leverage ratio or the review of EMIR, and which are not in the hands of ESMA. However, in line with paragraph 16, wide access to clearing is of particular importance to ESMA, therefore ESMA will continue to monitor and engage in the appropriate discussions where possible on what could affect access to clearing.

Responsibilities of the various participants in managing the risk of indirect clearing arrangements

25. Indirect clearing relies on a chain of entities performing their respective roles in order to provide access to clearing to the counterparty at the end of the chain. EU regulation and the RTS define the applicable requirements for the relevant entities performing these roles in order to ensure certain outcomes are achieved, in particular a certain level of protection.
26. Some respondents flagged some challenges with the management of the risk associated with indirect clearing services and commented on delimiting the responsibilities with regards to the management of risk as defined in the requirements, notably Articles 3(3) and 4(8) of the draft RTS of the consultation paper.
27. However, part of the risk of indirect clearing services is linked to the fact that there are so many layers in an indirect clearing chain, i.e. several consecutive intermediaries, and thus that the efficiency and the performance of the clearing chain is dependent on each and every link in the chain playing properly its role and managing the risk associated with it. Articles 3(3) and 4(8) are there to ensure that risks arising from facilitating indirect clearing arrangements are identified, monitored and managed to help safeguard each link in the chain.
28. Some respondents also commented on the gross model being dependent on the quality, the accuracy and the timeliness of the information being communicated throughout the chain in order to work. ESMA agrees with this and is of the opinion that this is precisely one of the risks that needs to be identified, monitored and managed by

the relevant entities in the chain. However, the draft RTS do not need to be prescriptive on how these risks are managed.

29. In addition, the requirements of the RTS look to preserve the anonymity of the commercial relationship between the client and its indirect client. Some respondents indicated that this anonymity would thus limit the ability for the entities up the chain to manage the risk. Indeed, only the necessary information is mandated to be passed to the next link in the chain and Article 4(8) includes a requirement to help ensuring that the client information is properly managed. ESMA thus understands that some of the information is not passed from the client to the clearing member and thus to the CCP, but this should be limited to information related to the identity of the indirect clients. Therefore, clearing members and CCPs would still need to identify, monitor and manage the risk based on the rest of the information that is available to them.
30. Finally, some comments were made suggesting harmonising the language of Articles 3(3) and 4(8). ESMA agrees that the text of these provisions can be aligned further. The revised drafting is reflected in the draft RTS in Annex.

2.3 Account structures and segregation models

31. The consultation paper was proposing that the choice of accounts should be between an omnibus account (the standard omnibus account that was already part of the EMIR RTS) and the gross omnibus account with some additional requirements that contribute to ensuring a level of protection with equivalent effect as referred to in Articles 39 and 48 of EMIR. Overall, a large amount of responses were supportive in many aspects with regards to the proposed choice of accounts, but some concerns expressed in the responses are also discussed below.

Individually segregated indirect account

32. To begin with, a few counterparties still commented on mandating the offer of an individually segregated indirect account in order to replicate the segregation offer stated in Article 39(3) of EMIR.
33. First of all, the gross omnibus indirect account with the additional requirements was determined in order to find the right balance between minimising the operational burden of the multiplicity of accounts implied with indirect individually segregated accounts (ISA) and ensuring an equivalent level of protection as referred to in Articles 39 and 48 of EMIR. Indeed the level of protection does not have to be identical. However, minimising the operational burden would make it more affordable, easier to implement, more scalable and in the end more likely to be offered than the indirect ISA.
34. In fact, some other respondents were supportive of ESMA's proposal of this new account precisely for that reason, i.e. that it would help increase the availability of indirect clearing arrangements that are compliant and that are meeting the objectives of the mandate.
35. Secondly, as discussed in the consultation paper, an indirect ISA would still be allowed to be offered.

Choice of accounts

36. Several respondents flagged, in line with the analysis of the consultation paper, that market demand with regard to ETD is in the majority for the net omnibus accounts. Whereas, with regard to OTC derivatives, they flagged that the market demand is for greater distinction between positions and collateral of separate clients or indirect clients, thus for gross omnibus and to some extent for individually segregated accounts. In general, these respondents were thus supporting the choice of accounts presented in the draft RTS, as it would fit with the respective degrees of distinction, between positions and collateral of separate clients or indirect clients, that are looked for in the ETD and the OTC derivative markets.
37. However some respondents were suggesting not mandating both accounts for both markets. Instead, they were suggesting to mandate in each draft RTS the one that corresponds to the traditional market demand for that market (the basic omnibus indirect account for ETD and the gross omnibus indirect account for OTC derivatives) and let the other choice of account (the gross omnibus indirect account for ETD and the basic omnibus indirect account for OTC derivatives) to be offered only where CCP and clearing members agree there is sufficient demand.
38. The first choice of accounts, the standard omnibus account, can be implemented in different forms, and that should give the necessary flexibility to adapt it to the needs of the respective markets. In particular, it doesn't specify whether this omnibus account has to be net or gross, and in fact this is consistent with EMIR as Article 39(2) does not specify net or gross either, as discussed in the consultation paper.
39. With regard to the second choice of account, it is a gross omnibus account with a set of minimum requirements, including in particular gross margin calculation by the CCP and the pass through of margin to the CCP. This has the objective to ensure a high level of distinction between indirect clients and a high level of protection for indirect clients, equivalent to the one granted to clients under EMIR.
40. Like Article 39 of EMIR that provides a choice of two accounts, the draft RTS provides a choice of two indirect client accounts, which helps fulfill the Level 1 mandate to provide an equivalent level of protection as referred to in Articles 39 and 48 of EMIR.
41. As a result, to comply with the draft RTS, the choice of accounts should include the gross omnibus indirect account (referred to in Article 4(2)(b) of the draft RTS) with all the additional requirements and an omnibus indirect account (referred to in Article 4(2)(a) of the draft RTS). This should leave enough flexibility to implement the second account type, the omnibus indirect account referred to in Article 4(2)(a) in the form most adapted to the demand in the respective markets.

Number of accounts at the CCP

42. Several respondents expressed their concerns or commented on the uncertainty as to the need to reproduce the proposed account structure at every level of the chain. In particular, they flagged the risk of a proliferation of accounts which was against the objective of operational simplification as desired with the gross omnibus proposal.
43. In addition, in response to the consultation, a large range of respondents of various profiles expressed support for a specific proposal, i.e. to request only one account at the CCP per clearing member, or per pair of clearing member and client, for each type

of account included in the choice detailed in the draft RTS. Therefore, with regard to accounts related to indirect clearing, this would mean two possible cases:

- a. two accounts at the CCP per clearing member, i.e. one basic omnibus indirect account where the positions and assets related to all the indirect clients of all the clients of the clearing member having chosen this account choice would be managed, and one gross omnibus indirect account where the positions and assets related to all the indirect clients of all the clients of the clearing member having chosen this account choice would be managed; or
 - b. two accounts at the CCP per pair of clearing member and client, i.e. one basic omnibus indirect account where the positions and assets related to all the indirect clients of one client of the clearing member having chosen this account choice would be managed, and one gross omnibus indirect account where the positions and assets related to all the indirect clients of the client of the clearing member having chosen this account choice would be managed.
44. In the case of a), indirect clients having chosen the same type of account structure and clearing through the same clearing member but through different direct clients would be managed at the level of the CCP in the same account.
 45. For example, in the situation of a clearing member with three clients and each client having four indirect clients, this would mean two accounts at the CCP: one basic omnibus indirect and one gross omnibus indirect account.
 46. In the case of b), indirect clients having chosen the same type of account structure and clearing through the same clearing member but through different direct clients would be managed in separate accounts at the level of the CCP, but in the same account where the other indirect clients having chosen the same type of account structure and the same client are managed.
 47. For example, in the situation of a clearing member with three clients and each client having four indirect clients, this would mean six accounts at the CCP: one basic omnibus indirect and one gross omnibus indirect account for the indirect clients of the first client, one basic omnibus indirect and one gross omnibus indirect account for the indirect clients of the second client, and one basic omnibus indirect and one gross omnibus indirect account for the indirect clients of the third client.
 48. In the case of long chains, under this proposal (regardless of case a or b), the structure would not need to be replicated throughout all levels. Even in the case b, the CCP would only distinguish between clients and not with further granularity.
 49. The approach from the start has been a slide down of responsibilities with requirements to ensure a protection of equivalent effect as referred to in Articles 39 and 48 of EMIR. In particular, for default management, in the case of indirect clearing then the clearing member is tasked with the responsibilities of default management, whereas in the case of client clearing it is the CCP.
 50. As a result, ESMA is of the opinion that the proposed simplification (in the number of accounts to be opened and maintained at the level of the CCP, in order to alleviate the operational effort) is not contrary to the slide down approach, as long as it can be

ensured that the appropriate separation of clients and indirect clients as applicable is done at the level of the clearing member.

51. However, the possibility of the default of the clearing member needs to be taken into account too when setting the requirements for indirect clearing. In this situation, when the CCP would be handling the default of the clearing member, the more segregation between the different clients (for the account of their indirect clients), the more likely it will be for the CCP to facilitate porting of the client's accounts to another clearing member or the leapfrog payment to each client.
52. The case a) described above (an account per clearing member but not per client) increases the chances of the CCP having to liquidate the account and return the proceeds to the insolvency practitioner of the defaulted clearing member as multiple indirect clients of multiple clients are managed in the same account. As a result, the approach of case a) would protect indirect clients less against the default of a clearing member. This situation would be even more acute in the case of a liquidation of the account following a double default, as the indirect clients would be exposed to the positions of other indirect clients, including indirect clients from a client they have not selected.
53. In the case b) described above (an account per clearing member and per client) the assets and positions of the indirect clients of a given client would be in a separate account from those of the indirect clients of another client of the clearing member. Therefore the chances would be increased that the CCP could port the entire account to another clearing member or that the CCP could do the leapfrog payment to that one individual client in charge of this pool of indirect clients, because each client would have its separate account. This structure would protect indirect clients more against the default of a clearing member.
54. In the case of the basic omnibus indirect account choice, indirect clients would have made the choice of the least segregation and the lower protections attached to this structure, therefore the approach of case a) would be in line with that choice.
55. However, in the case of the gross omnibus indirect account with the additional requirements, the indirect clients have made the choice for more segregation and more protection, therefore the approach of case b) would appear to be the most appropriate. This mix of approach for the two account types would go in the right direction of ensuring the appropriate balance between the objective of operational simplification and the mandate for an appropriate level of protection. This simplification is reflected in the draft RTS in Annex 3.3 and also illustrated in Annex 3.4.

Clarifications in the draft RTS

56. Some comments were made to clarify further in the Recitals and/or the Articles the items discussed in this section related to the account structures. For instance, some respondents commented on clarifying further that one indirect client's collateral value may be at risk from losses in another indirect client's positions in certain circumstances.

57. ESMA agrees that following the changes discussed in this section it was beneficial to review the drafting and the explanations, adding further clarification where possible. The draft RTS in annex have been updated accordingly.

2.4 Default management requirements

58. This section is about the requirements that relate to the management of the default of a client providing indirect clearing services. The consultation paper developed the explanation for the approach taken in the draft RTS, i.e. mirroring the drafting and approach of Article 48 of EMIR focusing on the obligation of means when drafting the relevant provisions for indirect clearing in the draft RTS. This topic continued to attract a lot of comments as was already the case in the previous consultations.

59. The requirements with regard to the choice of accounts and the requirements in relation to default management are covered in distinct provisions but they are inevitably linked. A further illustration of the proposed account structure and how it interacts with the default management requirements is proposed in Annex 3.4.3.

Insolvency regime

60. Many respondents commented on the approach of the obligation of means, with some expressing to some extent support for it. However, several respondents also argued that the issue of the potential conflict of law was still unresolved. In their responses they explained that porting, the leapfrog payment, procedures with steps to conduct porting or the leapfrog payment as well as contractual arrangements to keep proceeds away from the insolvency estate of the defaulting client may, and in many cases would, conflict with the applicable local insolvency regime, despite the requirement being limited to an obligation of means.

61. For several respondents, EMIR needs to be amended to provide clear protections with regard to default management, for example by integrating in the Articles themselves language along the lines of Recital 64 of EMIR. Alternatively, these respondents argued there is an important need for an EU harmonisation of insolvency regimes or client asset protection rules.

62. Without any of these changes, they state that it isn't possible to achieve the desired objective of an appropriate level of protection, one that would include porting rights and the leapfrog payment. Finally, they indicate that it should not be left to participants to establish procedures and contractual arrangements to overcome what EU regulation has failed to provide.

63. However, as these comments relate to decisions at level 1 or to national law, and are outside the scope of the RTS, respondents also commented on aspects that can be considered by ESMA at the level of the RTS.

Porting

64. First of all, a large number of respondents raised issues related to the re-introduction of the porting requirement. They understand that the requirement is for the most part limited to having procedures and triggering these procedures. However, they also

argue that as it is very unlikely that porting materialises (some say categorically that it could not), it is in fact counterproductive from a protection perspective to include this requirement.

65. First of all, they explain that during the period of time while porting is still being considered, the liquidation process is therefore delayed, which delay increases the market risk exposure (the longer the resolution for these cleared positions is postponed, the longer the time is during when the market can move). Secondly, they also argue that keeping a porting requirement is misleading for indirect clients that could therefore expect such an outcome, thus introducing the legal risk of some indirect clients challenging whether all the efforts have been conducted by the clearing member to try and make porting happen.
66. These respondents thus argue that the porting requirement should be removed as it introduces legal and default management risk. Some of them argue that if it is kept, it should be limited to the gross omnibus account, and that clarifications should be added to support the ability of the clearing member to make the appropriate decision from a risk management perspective. With respect to the latter, some respondents comment that this could include the ability to set a predefined and relatively short window when porting is considered, in line with Article 48 of EMIR. Some respondents also commented on getting further clarifications on what constitutes reasonable efforts by the clearing member to be deemed having met the obligation of means.
67. ESMA is of the opinion that in a net account it will be more difficult to port than in a gross account as it is more difficult to disentangle the portions of margin from the respective indirect clients, whereas in the gross omnibus account, by design it is distinguished. As a result, consistent with the difference of treatment between the two types of accounts with regard to the leapfrog payment, the porting requirement can also be limited to the gross omnibus indirect account. These changes are reflected in the draft RTS in Annex.
68. In addition, ESMA believes that the language of Article 4(8) of the draft RTS of the consultation paper (based on the last sentence of Articles 48(5) and 48(6) of EMIR where the reference to a “predefined transfer period” is made and where it is envisaged that porting could not take place “for any reason”), already provides sufficient flexibility a) to pre-define the time window when porting is considered, and b) not to affect the ability of clearing members to manage counterparty risk in the event of a default of a direct client.
69. Finally, as what is referred to as an obligation of means is primarily referring to an alignment of the drafting of the provisions with the corresponding Articles in EMIR, the RTS cannot at the same time deviate from the EMIR text by introducing additional norms as it would introduce the risk of undermining the intent of the Level 1 text. As a result, further clarifications, which would in fact be limitations, are not considered as part of the draft RTS text.

Leapfrog payment

70. To begin with, the same comment was made with regard to the obligation of means in the context of the leapfrog payment as with porting, i.e. the need for further guidance or

clarification on what would meet the requirement of the obligation of means. However, the rationale and the conclusion are the same as in the above paragraph 69.

71. Following on from the topic of the leapfrog payment, the consultation paper complemented the approach referred to as the obligation of means (that cannot guarantee the desired outcome in all cases) with additional safeguards. In line with the spirit of Article 48(7) of EMIR which refers to the return of proceeds to the defaulting entity “for the account of” the entity after the defaulting entity, the draft RTS contained the requirement to have contractual arrangements ensuring the liquidation proceeds do not form part of the insolvency estate.
72. However, this provision attracted a certain amount of comments. Some respondents asked that it is removed because it goes beyond EMIR drafting, because these contractual arrangements would be bespoke and not consistent across countries, thus not scalable and prohibitively costly, and last but not least because they would potentially conflict with the applicable insolvency law.
73. ESMA is of the opinion that these contractual arrangements can provide safeguards and that these contractual arrangements would contribute to how entities comply with the requirement of returning the proceeds “for the account of” the indirect client. However, the draft RTS can simply mirror the EMIR text and thus being more open to how entities will prepare for fulfilling the draft RTS requirement (the proceeds “for the account of” the indirect client). This change is reflected in the draft RTS in Annex.
74. Finally, some respondents, representatives of clearing members, raised concerns with what is expected in terms of know-your customer procedures in the context of the leapfrog payment. Indeed, the identity and some important operational details about the indirect clients of the direct client would only become known at the time of the default of the direct client. This could potentially stand in the way of a timely leapfrog payment.
75. However, it is not for this draft RTS to establish client related due diligence requirements as this relates to other applicable rules. Moreover, this regulation is not intended to undermine client due diligence checks and this is not the only case where different sets of rules could complement each other. Additionally, the client is an authorised credit institution, investment firm or an equivalent third country credit institution or investment firm, therefore it is expected the clients would themselves have to comply with certain due diligence standards, which should limit the problematic situations related to who the indirect clients are. But again, this regulation is not intended to replace the applicable rules on this matter.

2.5 Long chains

76. The consultation paper presented the proposed approach to address the case of long chains, which was based on an extension of the requirements applicable to clients to indirect clients facilitating themselves indirect clearing services. However, the consultation paper acknowledged that the task was already complex to establish requirements that fulfil the mandate and that can be implemented, and thus that this equation is even more complex the more layers were added to the chain. The

consultation paper asked for greater input on this topic and possible alternative approaches with an additional question.

77. Many respondents commented on the topic of long chains, primarily to focus on the uncertainty around the proposal or the need for further clarification. Some also commented on reconsidering the level of protection that should be afforded to entities at each link of the chain rather than solely focusing on the end counterparty. Some commented on how the default of an intermediary indirect client should be handled as under the RTS the clearing member is tasked with the management of the default of a client but in this case it should be the entity before the defaulting intermediary indirect client.
78. A few suggestions were made but none appeared to be the silver bullet. The first suggestion was that the requirements should only apply to the first 4 entities in the chain, sometime making a reference to the somewhat similar approach of the MiFIR consultation paper of December 2014.
79. The second suggestion was to translate the requirements along the chain, i.e. that a client or indirect client providing indirect clearing services to an indirect client would be subject to the client requirements and that the entity before, even if a client or indirect client, would be subject to requirements of the clearing member.
80. The third suggestion was to recognise the role of intragroup transactions and thus consider that two consecutive entities from the same group in the chain do not constitute different layers, thus reducing conceptually the length of some longer chains. The draft RTS would thus need to set requirements for entities that would be somehow dependent on other entities of the same group being involved.
81. For example, a group with a global clearing member clearing through a local affiliate would still be handling the requirements applicable to the clearing member, for its entities, and not those of a direct client.
82. As a result, following the multiple consultations, there does not appear to be any unambiguous approach that can ensure the related requirements would meet the objectives of the EMIR and MiFIR mandates. ESMA is thus of the opinion that chains with more than four layers would not comply with the EMIR and MiFIR requirements and thus should not be permissible.
83. However, ESMA sees some merits with the third approach. It considers that indeed, when there are several consecutive entities from the same group, these can be considered to form the same layer under certain scenarios and as long as the objectives of the mandate are met. This means that only in these cases there could be long chains with more than 4 entities but with still 4 layers.
84. To begin with, with regards to the segregation requirements, in the case of long chains with consecutive entities from the same group, the draft RTS has been amended to ensure segregation between cleared proprietary positions and cleared positions resulting from the provision of indirect clearing services is present at all levels of the long chain.
85. Yet, in order to avoid any increased complexity in these long chains and maintain a manageable flow of information, both under normal circumstances as well as under

stressed situations or situations of a default, this structure with successive entities forming the same layer is only accommodated for two entities maximum from the same group.

86. In any case, ESMA believes there should not be such a strong need for having more than two entities from the same group to be involved in these long chains. In general, the need for several entities from the same group to be involved in a clearing chain is to rationalise and centralise the clearing services across the activities in one entity, to simplify the commercial relationship between two entities, or to facilitate arrangements with entities established in other jurisdictions.
87. Indirect clearing chains are sometimes represented as tree diagrams, with each layer having many clients of its own, and so on. However, in the case of long chains with successive entities from the same group, the consecutive entities play more the role of a conduit of cleared activity or a pass-through of cleared activity rather than a succession of one-to-many clearing relationships in tree diagrams. As a result, two entities from the same group should be sufficient and would contain the complexity that can increase with one-to-many client relationships.
88. The intention of permitting successive entities from the same group is to facilitate access to clearing for certain smaller counterparties that rely on these long chains in order to access some ETD markets. However, the intention is not to allow groups to add layers artificially. As a result, a condition is added in the draft RTS so that this group approach is permitted only when the entities after the clearing member and the other entity in the clearing member's group are not part of the same group. For instance, an affiliate of the clearing member in the fourth position in the clearing chain (the client of a client of the clearing member) would not meet the conditions of the draft RTS and could not be acting as a client for the provision of indirect clearing services instead of the entity before it.
89. Furthermore, in order for the draft RTS to meet the objective of the mandate not to increase counterparty risk, the addition of entities in the permissible indirect clearing chains are only accommodated for indirect clients that have made the informed choice of the least segregation and protection of the account structures offered, i.e. the basic omnibus indirect clearing account choice.
90. Indeed, the provisions of the draft RTS are designed so they come in support of porting and the leapfrog payment for the indirect clients that have opted for the gross omnibus indirect account. With more entities in the clearing chain, these indirect clients would become exposed to the default of more intermediaries. In addition, with multiple entities from the same group, be it the group of the clearing member or the group of the client, in the clearing chain, it would be less likely that if one entity of the group defaults the other entity would not be affected and porting or the leapfrog payment could be facilitated.
91. However, this exception to chains of four layers for allowing arrangements with more than four entities should still ensure that the indirect clients at the end of the chain are offered a choice of the two types of mandated accounts. Allowing long chains only for the basic choice of account should not come at the expense of the gross omnibus indirect account structure and the protection offered to indirect clients.

92. Therefore, these exceptions would still require the clearing member and the client groups, through one of their entities, to offer the possibility for the indirect client of a gross omnibus indirect account under a 4 entity arrangement. Given the comments developed in paragraph 10 and thus the EU CCP nexus, the ability to offer 4 entity arrangements with the gross omnibus indirect account is not expected to be a limiting factor as the potential need for local entities in addition to more international oriented entities is less relevant in the case of indirect clearing arrangements to clear at EU CCPs.
93. Last but not least, besides defining the conditions that long chains need to meet, the draft RTS also details the requirements that apply to each entity involved in such a long chain. In addition to the requirements defined in the first Articles of the draft RTS that apply respectively to the CCP, the clearing member and the client (as per the meaning of EMIR), the last Article specifies the additional requirements that apply to the entities involved in long chains, intermediate indirect clients included.
94. The approach that has been followed is to require the doubling of responsibilities for the intermediate entities, i.e. the addition of responsibilities that are typically the responsibilities of clearing members (particularly the management of the default of the entity after) and of responsibilities that are typically the responsibilities of clients providing clearing services to their client (particularly ensuring the appropriate level of segregation and protection is offered to the end counterparty, the end indirect client).
95. This proposal has the objective to ensure an appropriate and equivalent level of protection with this doubling of responsibilities. In this case also, this is an approach that corresponds to some of the market practice, for instance it is typically the entity before the defaulting entity that manages the default.
96. The related changes are reflected in the draft RTS in Annex 3.3. An illustration of these long chains with successive entities from the same group has been provided in Annex 3.4.4.

2.6 Additional draft provisions

97. Beyond the requirements discussed and covered in the previous sections, a few additional items were considered in the consultation paper.

Assign to standard account

98. The consultation paper introduced a provision to allow the client to assign the indirect client to one of the proposed accounts after reasonable efforts to get the indirect client's election and the latter has not provided this information.
99. There was broad support from practically all respondents for this provision. However, some commented with some suggestions to ensure the choice is still offered for the indirect client when it is ready to make a choice. One respondent was suggesting requiring procedures to explicitly confirm the type of arrangements chosen and have a rapid and efficient way to switch to the finally elected account when asked by the indirect client.

100. First of all, the draft RTS already contains a provision to inform the indirect client of the assignment by default and the risk associated with it. Secondly, the choice of accounts is always offered to the indirect client as per the objective of the draft RTS. As a result, ESMA is of the opinion that these concerns are already addressed in the draft RTS.

Excess collateral

101. The consultation paper specified that under the ESMA proposal, the excess collateral would be treated in accordance with the contractual arrangements between the relevant parties.

102. For this proposal as well, there was broad support from respondents. However, some respondents consider that was a departure from the treatment of excess collateral in the case of individually segregated accounts in the case of client clearing. Others, primarily representatives from CCPs, commented on making sure the proposal did not evolve to a gross omnibus with excess.

103. Indeed, this is not the case, the second choice of account is not a model with excess. ESMA understands that the allocation of excess collateral in the context of indirect clearing can be challenging and prefers to leave it to the contractual arrangements between all parties to decide on its treatment.

3 Annexes

3.1 Annex I - Legislative mandates to develop technical standards

3.1.1 Legislative mandate to develop technical standards under EMIR

Article 4 of Regulation (EU) No 648/2012

Clearing obligation

4. In order to ensure consistent application of this Article, ESMA shall develop draft regulatory technical standards specifying the contracts that are considered to have a direct, substantial and foreseeable effect within the Union or the cases where it is necessary or appropriate to prevent the evasion of any provision of this Regulation as referred to in paragraph 1(a)(v), and the types of indirect contractual arrangements that meet the conditions referred to in the second subparagraph of paragraph 3.

ESMA shall submit those draft regulatory technical standards to the Commission by 30 September 2012.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1095/2010.

3.1.2 Legislative mandate to develop technical standards under MiFIR

Article 30 of Regulation (EU) No 600/2014

Indirect Clearing Arrangements

2. ESMA shall develop draft regulatory technical standards to specify the types of indirect clearing service arrangements, where established, that meet the conditions referred to in paragraph 1, ensuring consistency with provisions established for OTC derivatives under Chapter II of Commission Delegated Regulation (EU) No 149/2013.

ESMA shall submit those draft regulatory technical standards to the Commission by 3 July 2015.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in this paragraph in accordance with Articles 10 to 14 of Regulation (EU) No 1095/2010.

3.2 Annex II - Cost-benefit analysis

3.2.1 Executive Summary

1. Pursuant to Article 10(1) of the Regulation establishing ESMA, ESMA is empowered to develop draft regulatory technical standards where the European Parliament and the Council delegate power to the Commission to adopt regulatory technical standards (RTS) by means of delegated acts under Article 290 TFEU in order to ensure consistent harmonisation in the areas specifically set out in the legislative acts within the scope of action of ESMA. The same article obliges ESMA to conduct open public consultations on draft RTS and to analyse the related potential costs and benefits, where appropriate. Such consultations and analyses shall be proportionate in relation to the scope, nature and impact of the draft RTS.
2. The purpose of the two draft RTS presented in Annex of the final report is to specify the requirements to a) ensure that indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR, and to b) ensure consistency between the provisions of the two draft RTS.
3. This document has four sections. The first section is the introduction, which sets out the background for the two RTS. The second section details the baseline and thus explains the starting point for assessing the incremental rule related to ESMA's draft RTS. The third section covers the stakeholders, which have been identified as being CCPs, clearing members, clients, indirect clients as well as any market participants involved in indirect clearing flows. The final section provides an overview of the benefits and costs associated with the proposals set out in the RTS.
4. In practice, it may sometimes be very difficult to disentangle the effects of the Level 1 provisions, for which an impact assessment covering the general aspects of the Regulation has been already performed and published by the European Commission, and the effects of the Level 2 provisions.
5. For instance, Level 1, through Article 4(3) of EMIR and Article 30(1) of MiFIR, already requires that indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR. These Level 1 requirements can already represent new costs for CCPs, clearing members, clients and indirect clients to put in place new indirect clearing arrangements or amend existing ones (along with necessary changes to the associated systems, procedures, training, etc.) in order for the arrangements to be compliant with the Level 1 requirements.
6. The costs associated to the requirements that ESMA is tasked to set in the draft RTS can thus be already covered for some part in the costs required in order to comply with the Level 1 requirements. They can be marginal cost increases if they correspond to small additions or changes to existing processes complying with Level 1, or be important costs if they require achieving the same goal of Level 1 requirements in a different manner than currently done.

7. As a result, providing a level of flexibility in the text of the draft RTS about the means to achieve the objective of Level 1 and the RTS, to the extent possible, has been an important component in the way the standards have been drafted.
8. For instance, the basic choice of account in Article 39 of EMIR is an omnibus account with some flexibility on how this omnibus account can be implemented. Following a similar approach, the basic choice of account in the draft RTS is an omnibus account which also leaves flexibility in how it is implemented, for instance it does not specify whether positions have to be managed in a net or gross basis by the CCP or the clearing member.
9. Another such example is the approach with long chains. The draft RTS has been designed in a way that allows some indirect clearing arrangements with more than 4 entities and that use an account in accordance with the basic omnibus indirect account of the RTS, which are typically the arrangements used in long chains for ETD. This approach of providing flexibility where possible, should allow stakeholders to leverage to the extent possible what has been developed for complying with Level 1.

3.2.2 Introduction

10. Article 4(3) of EMIR and Article 30(1) of MiFIR require that indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR.
11. Under Article 4(4) of EMIR and Article 30(2) of MiFIR, ESMA is required to develop draft RTS, in relation to OTC derivatives and ETD respectively, to specify the types of indirect clearing arrangements that meet the conditions referred to in Article 4(3) of EMIR and Article 30(1) of MiFIR.
12. In addition, for the MiFIR RTS, Article 30(2) of MiFIR requires consistency with the provisions on indirect clearing arrangements established for OTC derivatives under EMIR.
13. As explained in the first section of the final report, the draft RTS under EMIR that is presented in the final report is an amending RTS of Commission Delegated Regulation (EU) No 149/2013, such that the two draft RTS presented in the final report being considered together, the consistency requirement can be met.
14. The analysis that follows takes into account the responses received to the MiFIR discussion paper, the MiFIR consultation paper and the Cost Benefit Analysis questionnaire distributed by ESMA at that time, the second consultation paper which covered indirect clearing arrangements under both EMIR and MiFIR.

3.2.3 Baseline

15. With regard to the MiFIR RTS, it is to be noted that MiFID I did not explicitly establish any provisions regarding indirect clearing arrangements. Therefore the baseline is Article 30 of MiFIR, which requires that indirect clearing arrangements do not increase

counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR.

16. With regard to the draft EMIR RTS, the draft RTS is an amending RTS of Commission Delegated Regulation (EU) No 149/2013. As a result, the existing EMIR RTS could be considered the baseline as its requirements are in force. This is the baseline that was indicated in the second consultation paper that considered together the requirements under EMIR and MiFIR together.
17. However, as discussed in the consultation papers, it appears that no indirect clearing offering has developed for OTC derivatives. Therefore, there should be limited or no impact to stakeholders from the amendments. In fact, the amending RTS has exactly the opposite objective, the draft RTS amending the EMIR RTS is presented in order to ensure the EMIR RTS does fulfil its objective, and because of the consistency requirement, that the MiFIR RTS can also fulfil its objective.
18. In other words, with regard to the EMIR RTS, it can also be considered that the baseline is also the Level 1 requirement. EMIR also requires that indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR. This was also reflected in the answers to the second consultation paper.
19. Indeed the comments on the costs and benefits were sometimes nuanced between OTC derivatives and ETD not because the baseline for OTC derivatives was proposed to be Commission Delegated Regulation (EU) No 149/2013, but because a large part of the ETD market has relied traditionally on indirect clearing, whereas it has not been the case with OTC derivatives. The comments from respondents were in regard to the cost and benefits related to compliance with the amended EMIR RTS and the new MiFIR RTS and not with regard to the changes compared to Commission Delegated Regulation (EU) No 149/2013.
20. The purpose of this document is thus to assess the incremental obligation of ESMA's RTS against the Level 1 baseline described above.

3.2.4 Stakeholders

21. Article 1(b) of Commission Delegated Regulation (EU) No 149/2013 defines indirect clearing arrangement as the set of contractual relationships between the CCP, the clearing member, the client of the clearing member and the indirect client, that allows the client of a clearing member to provide clearing services to an indirect client. The draft RTS presented in the final report maintain this definition, although they contain an Article on long chains that extends the definition of which counterparties are indirect clients.
22. Stakeholders thus include CCPs, clearing members, clients and indirect clients that are involved in the processing of cleared derivatives through indirect clearing arrangements but more broadly all market participants that are involved in indirect clearing flows.

23. Most of the costs should arise from the Level 1 provisions. CCPs, clearing members, clients and indirect clients may face some one-off as well as on-going costs arising from the implementation of EMIR and MiFIR Level 1 provisions on indirect clearing arrangements and to ensure that these arrangements do not increase counterparty risk and to ensure that through these arrangements the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR.
24. Other market participants that are involved in indirect clearing flows may also face some one-off and on-going costs to adapt to the arrangements that CCPs, clearing members, clients and indirect clients put in place or modify to ensure that they are compliant.

3.2.5 Cost benefit analysis

Requirements for indirect clearing arrangements

Policy Objective	Setting the requirements ensuring that indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR
Technical proposal	<p>In order to meet the objective of the mandate, i.e. with respect to the requirements on segregation and default management procedures and the requirement not to increase counterparty risk, the draft RTS present a set of requirements that provide altogether an equivalent level of protection as referred to in Articles 39 and 48 of EMIR, but not an identical one.</p> <p>The requirements need to be considered altogether as it is the cumulative effect of the requirements that can ensure the protection is equivalent. However, the main components contained in these requirements are indicated below.</p> <p>First of all, in terms of account structure, the draft RTS ensures segregation between the proprietary activity of the entities facilitating indirect clearing services and the clearing activity of the indirect clients. In addition, the draft RTS includes a choice of two accounts with different levels of distinction between the positions and assets of the indirect clients.</p> <p>It includes a basic omnibus indirect account that provides flexibility on how it is implemented, in particular whether in a net or gross basis. It also includes a gross omnibus indirect account with specific requirements, including the pass through of margin all the way to the CCP, in order to ensure a greater separation of clearing activity between indirect clients, although being managed in a single account, and to ensure an amount of margin equivalent to the amount that would have been required in an individually segregated account, thus increasing the level of protection.</p>

	<p>Secondly, in terms of default procedures, the draft RTS requires procedures to properly manage the default of the client. In the case of the gross omnibus indirect account, the procedures include the steps to conduct porting and the leapfrog payment, and the requirements put the emphasis on the obligation of means, in line with the EMIR text. When porting cannot work, liquidation can be conducted, and when the leapfrog payment cannot be completed, then the proceeds from the liquidation are to be returned to the client for the account of the indirect clients.</p> <p>In the case of the basic omnibus account, as there are less provisions than with the gross omnibus indirect account to ensure enough distinction and identification of the positions and assets of each indirect client, the procedure is centered around the prompt liquidation of the account, in order not to delay the management of the default and to minimise the potential loss.</p> <p>See Articles 2, 3, 4 and 5 of the draft RTS for more details.</p>
<p><i>Benefits</i></p>	<p>Ensuring an equivalent level of protection as referred to in Articles 39 and 48 of EMIR, by setting requirements that on the one hand minimise the operational burden and that on the other hand, take into account the issue of the potential conflict of law with regard to insolvency, in particular when some of the entities involved in the indirect clearing arrangement are located in a third country.</p> <p>In particular, the choice of accounts provides a certain level of flexibility and takes into account the range of accounts that have been developed in the market for each type of derivatives, ETD on one side and OTC derivatives on the other side.</p> <p>Indeed, ETD market participants have traditionally relied on arrangements based on a net omnibus account, whereas cleared OTC derivatives have seen a greater demand for distinction between the positions and assets of each entity, including gross omnibus accounts. Both markets can thus be accommodated through the required choice of accounts defined in the draft RTS.</p> <p>On the one hand, this choice of accounts provides flexibility in how the arrangements in the two markets are implemented but as well in how indirect clearing arrangements can evolve, possibly with more activity towards gross omnibus accounts in the future. And on the other hand, this choice of account enables consistency between the two draft RTS, although they cover different markets.</p> <p>In addition, the draft RTS contains detailed requirements for the accounts to be opened and maintained at each link in the chain, with the objective to limit their number and thus decrease the complexity and the operational</p>

	<p>risk of a proliferation of accounts, while at the same time ensuring an appropriate level of segregation and thus number of accounts to provide an equivalent level of protection to indirect clients in the case of the default of an intermediate entity providing indirect clearing services.</p> <p>Finally, with regard to the default procedures, the approach of the RTS to align its language to the EMIR text enables to take into account the problem of potential conflict of law, and thus eases the implementation of these requirements in comparison to the requirements set in Commission Delegated Regulation (EU) No 149/2013.</p>
<p><i>Costs to regulator:</i></p> <ul style="list-style-type: none"> • One-off • On-going 	<p>Incremental costs for regulators with regards to these standards in comparison to the Level 1 requirements should be minimal, regulators should be able to absorb any costs arising from monitoring compliance with these standards into their regular supervisory functions.</p>
<p><i>Compliance costs:</i></p> <ul style="list-style-type: none"> • One-off • On-going 	<p>CCPs, clearing members, clients and indirect clients that had arrangements already in existence and permitted under the new standards should not incur one-off costs and only marginal ongoing costs to monitor they are compliant with the new requirements.</p> <p>However, as there were no EU requirements before EMIR and MiFIR as discussed in the baseline section, it is likely that some elements of the existing indirect clearing arrangements would need to be reviewed against the requirements of Level 1. Although, this may not have yet taken place.</p> <p>With respect to ETD, MiFIR has not entered into force yet. With respect to OTC derivatives, on the one hand, the clearing obligation has only recently entered into force and the phase-in starts with clearing members that have access to CCPs, and on the other hand, it does not appear that any indirect clearing offering has developed.</p> <p>Therefore, for both ETD and OTC derivatives, it is likely that for many entities involved in indirect clearing, the bulk of the efforts to ensure they are compliant with the Level 1 requirements on indirect clearing arrangements has not taken place yet, and that, in line with the responses to the consultations, they have been waiting for further legal certainty on the Level 2 requirements.</p> <p>As a result, it is likely that CCPs, clearing members, clients and indirect clients may incur one-off and ongoing costs, in particular related to IT, legal, training and staff costs, in order to comply with Level 1, but in a manner where they have clarity on the Level 2 requirements.</p> <p>Therefore, one-off costs will arise from Level 1, i.e. from the necessary changes to ensure their indirect clearing arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR, and will likely include the incremental costs incurred in order to comply with the requirements set in the RTS. The</p>

	on-going costs will arise from the continuous supervision/update/monitoring of their indirect clearing arrangements against the new standards.
<i>Costs to other stakeholders</i>	Other market participants that are involved in indirect clearing flows for cleared derivative transactions may also incur similar costs to CCPs, clearing members, clients and indirect clients to adapt to the new standards, but of a relatively smaller order of magnitude as the requirements apply and are mostly relevant to CCPs, clearing members, clients and indirect clients.
<i>Indirect costs</i>	<p>If some CCPs, clearing members, clients have to modify significantly their arrangements (and the associated systems, procedures, training, etc.) to meet the new standards, then there is a risk that some will stop providing services to certain parts of the derivative market or that they will need to pass the costs to their indirect clients in respect to these parts of the derivative market.</p> <p>For small firms, some of these costs may constitute a barrier of entry.</p>

Requirements for long chains

Policy Objective	Setting the requirements for indirect clearing arrangements that involve more entities than in the current definition of Commission Delegated Regulation (EU) No 149/2013, to ensure these arrangements do not increase counterparty risk and ensure that the assets and positions of the counterparty benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of EMIR
Technical proposal	<p>In order to ensure that long chains don't increase counterparty risk and provide an equivalent level of protection as referred to in Articles 39 and 48 of EMIR, the draft RTS contain conditions in order to limit the types of long chain arrangements and contain specific and additional requirements for the entities involved in these long chains in order to provide clarity on the requirements each counterparty has to comply with.</p> <p>The two main conditions that long chains need to meet are related to the type of account allowed to be used in these long chains and the relationship between the entities involved in these long chains.</p> <p>Indeed, the draft RTS specify that long chains are permissible when the basic omnibus indirect account is used. Allowing the gross omnibus indirect account in these long chains would weaken the protections it is meant to provide.</p> <p>The draft RTS specify also that there can only be two consecutive entities from the same group in the long chain, i.e. two entities from the group of</p>

	<p>the clearing member and/or two entities from the group of the client. Not Allowing longer chains and more entities from the same group would not ensure counterparty risk is not increased and protections are not weakened in these long chains.</p> <p>In the case of long chains that meet these conditions, the draft RTS set additional requirements as there are more entities involved than in the standard four-entity indirect clearing chains and because intermediate entities have a mix of responsibilities, in fact the doubling of responsibilities.</p> <p>Indeed, intermediate entities are subject to requirements that clearing members are subject to, and they are also subject to requirements that clients are subject to. They are responsible for managing the default of the intermediate entity that is their immediate client and they are responsible for ensuring the appropriate segregation and protection is offered to the end indirect client.</p> <p>See Article 6 of the draft RTS for more details.</p>
<p><i>Benefits</i></p>	<p>Ensuring that long chains benefit from the objective of the mandate of a certain level of protection, and at the same time, ensuring that such long chains are available to many market participants who rely on such long chains to clear their derivatives and thus access certain derivative markets.</p> <p>The draft RTS build on the long chain arrangements that exist currently in practice. The requirements thus take into account the types of long chains and the responsibilities that are used in practice.</p> <p>Indeed, long chains are often used in the ETD market, which has traditionally been relying on a net omnibus account. The draft RTS provide flexibility in how the required basic omnibus indirect account is implemented and should allow catering for the traditional ETD market.</p> <p>In addition, when long chains in the market rely on more than four entities, it is usually the case because there are several entities from the same group involved. For instance, in the group of the clearing member there can be an entity acting as a global provider of clearing services which may result in involving this entity in addition to the affiliate entity being the member of the CCP.</p> <p>Similarly, a client can also involve an affiliate, depending on the entity that has the relationship with the clearing member and the entity that has the relationship with its client, the indirect client. Going through these multiple entities can also be a consequence of the different jurisdictions where the CCP, the clearing member, the client and the indirect client are established. The draft RTS, by allowing long chains with two entities from the group of the clearing member and/or the group of the client, should</p>

	<p>provide sufficient flexibility for the types of long chains that are relevant in the market.</p> <p>Finally, the requirements that apply to the intermediate entities also reflect the responsibilities that can exist in the current practice. For instance, it is usually the entity before the entity defaulting that handles the default.</p> <p>Feeding to the extent possible some of the elements from the current market practice in how the requirements are set should allow to maintain a level of access to clearing via indirect clearing arrangements, in this case long chains, and thus a level of access to the trading of the related derivatives.</p>
<p><i>Costs to regulator:</i></p> <ul style="list-style-type: none"> • One-off • On-going 	<p>Incremental costs for regulators with regards to these standards in comparison to the Level 1 requirements should be minimal, regulators should be able to absorb any costs arising from monitoring compliance with these standards into their regular supervisory functions.</p>
<p><i>Compliance costs:</i></p> <ul style="list-style-type: none"> • One-off • On-going 	<p>CCPs, clearing members, clients and indirect clients that had long chain arrangements already in existence and permitted under the new standards should not incur one-off costs and only marginal ongoing costs to monitor they are compliant with the new requirements.</p> <p>However, the comments on the costs for indirect clearing arrangements to comply with the EU Regulation requirements that are discussed in the previous table also apply to long chains.</p> <p>Yet, as discussed in this table, the additional requirements for long chains reflect to the extent possible some of the elements from the current market practice. This should help minimise the additional costs for long chains, in comparison to the costs entities would incur for their standard four entity indirect clearing arrangements to comply with the new requirements and discussed in the previous table.</p> <p>However, for the additional entities involved in long chains, it could be argued that the costs incurred by CCPs, clearing members, clients and indirect clients to comply with the new requirements would also be incurred in a similar manner. Yet, long chains imply that the additional entities involved are affiliates of the group of the clearing member or the group of the client. Therefore, even if involving more entities would imply more costs for a group, there should be some economy of scale in the costs across the entities.</p>
<p><i>Costs to other stakeholders</i></p>	<p>Other market participants that are involved in long chains for cleared derivative transactions may also incur similar costs to CCPs, clearing members, clients and indirect clients to adapt to the new standards, but of a relatively smaller order of magnitude as the requirements apply and are mostly relevant to CCPs, clearing members, clients and indirect clients.</p>

<i>Indirect costs</i>	<p>If some CCPs, clearing members, clients have to modify significantly their arrangements (and the associated systems, procedures, training, etc.) to meet the new standards on long chains, then there is a risk that some will stop providing services to certain parts of the derivative market or that they will need to pass the costs to their indirect clients in respect to these parts of the derivative market.</p> <p>For small firms, some of these costs may constitute a barrier of entry.</p>
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3.3 Annex III - Draft RTS

3.3.1 Draft RTS on the indirect clearing arrangements under EMIR

COMMISSION DELEGATED REGULATION (EU) No .../..

of XXX

[...]

Amending Commission Delegated Regulation (EU) No 149/2013 with regard to regulatory technical standards on indirect clearing arrangements of [] (text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories, and in particular Article 4(4) thereof,

Whereas:

- (1) An indirect clearing arrangement should not expose a CCP, clearing member, client or indirect client to additional counterparty risk and the assets and positions of the indirect client should benefit from an appropriate level of protection. It is therefore essential that any type of indirect clearing arrangements comply with minimum conditions for ensuring their safety. To that end, the parties involved in indirect clearing arrangements should be subject to specific obligations and indirect clearing arrangements should only be permissible provided that they meet the conditions defined in this Regulation. Such arrangements extend beyond the contractual relationship between indirect clients and the client of a clearing member that provides indirect clearing services.
- (2) As the assets and positions of the counterparty in indirect clearing arrangements must benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories⁵, the concept of

⁵ OJ L 201, 27.7.2012, p.1.

indirect client, stemming from that Regulation but not defined therein, is pivotal for this Regulation and should be defined herein.

- (3) Regulation (EU) No 648/2012 requires a CCP to be a designated system under Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems⁶. This implies that clearing members of CCPs should qualify as participants within the meaning of that Directive. Therefore, to ensure an equivalent level of protection to indirect clients as granted to clients under Regulation (EU) No 648/2012, it is necessary to ensure that clients providing indirect clearing services are credit institutions, investment firms, or equivalent third country credit institutions or investment firms.
- (4) Indirect clearing arrangements involve by design a larger number of entities in comparison to direct clearing arrangements. The larger number of intermediate entities in indirect clearing arrangements means there is a higher degree of intermediation activity between the CCP and the indirect client. Additional intermediate entities and the resulting increased intermediation activity require additional operational steps, additional accounts as well as more complex technological solutions and processing flows. The increased complexity associated to the higher number of entities between the CCP and the indirect client compared to client clearing arrangements should be mitigated with requirements for an alternative and operationally simpler choice of account structures for indirect clearing arrangements than for client clearing arrangements.
- (5) For client clearing, Regulation (EU) No 648/2012 specifies two account structures. The first account structure is an omnibus account. This account structure is the less complex structure that can be required while still ensuring a separation between the collateral and positions of the indirect client and the collateral and positions of the client providing clearing services. The requirement for this first account structure should therefore be mirrored for indirect clearing arrangements.
- (6) The second account structure is an individually segregated account, which requires separate accounts for each client and thus an increased number of operational processes to manage all the separate accounts than if the clients were managed in a single account. Requiring such an account structure in the case of indirect clearing services would multiply the number of necessary accounts and related operational processes, raising the complexity, cost and operational risk of indirect clearing arrangements.
- (7) Alternatively, a gross omnibus indirect account structure with a mechanism of a transfer of margin from the indirect client all the way to the CCP would allow to achieve an equivalent distinction between the collateral and the positions held for the account of a

⁶ OJ L 166, 11.6.1998, p. 45.

specific indirect client from the collateral and the positions held for the account of the direct client or other indirect clients, while requiring a much simpler account structure. Such an alternative account structure and processing would reduce the number of accounts to be opened and maintained and therefore the related number of operational steps to margin and settle collateral in these accounts. This structure would reduce the cost and complexity compared to individually segregated accounts, while still permitting to distinguish the collateral and the positions of different indirect clients and therefore ensuring an equivalent level of protection as an individually segregated account. Although this would not preclude individually segregated indirect accounts to also be offered.

- (8) In order to ensure that the same amount of margin would be called with a gross omnibus indirect account structure as if the indirect client were using an individually segregated indirect clearing account structure, the CCP would need information on the positions held for the account of the indirect client in order to calculate the associated margin call on an indirect client by indirect client basis.
- (9) Margining on a gross basis would imply that the netting of positions of different indirect clients in the same gross omnibus indirect account, or the use of the margin of an indirect client to cover for the margin requirement of another indirect client in the same gross omnibus account, could not be performed when recording the positions of each indirect client and when calculating and calling the corresponding margin requirements.
- (10) Margins are the first line of defence in the case of a default and maintaining margins at the level of the CCP protects the clients from the default of the clearing member. Requiring passing margins all the way to the CCP would protect the indirect client not only from the default of a client, but also from the default of the clearing member.
- (11) Any collateral received above the margin amount called by the clearing member should be treated in accordance with the relevant terms of the indirect clearing arrangements.
- (12) As for client clearing, where, following the failure of a clearing member that facilitates clearing services, the CCP should be prepared to transfer the clients positions to an alternative clearing member and to liquidate them if necessary, for indirect clearing, the clearing member should have procedures to facilitate the transfer of indirect clients' positions to an alternative client following the failure of a client that facilitates indirect clearing services. The clearing member should also have procedures to liquidate the positions and assets of the indirect clients and to return the liquidation proceeds to the indirect clients when known. And when the client that fails has been facilitating clearing services with a gross omnibus indirect account structure, the clearing member should commit to trigger these procedures.
- (13) Under the gross omnibus indirect account structure, the information on the positions held for the account of each indirect client is passed daily to the different entities involved in the

indirect clearing arrangement without the exact identity of the indirect clients. Therefore, safeguards should be put in place so that in the case of the default of the client, the information on the identity of the indirect clients can become known to the clearing member so that the identification of which assets and positions belong to which indirect client can be done.

However, with the basic omnibus indirect account structure, the information on the positions held for the account of each indirect client is not passed on, so in the case of the default of the client, the identification of which assets and positions belong to which indirect client might not be unequivocally and quickly determined. In such situation porting would be unrealistic and the time taken to attempt porting would introduce delays and risk to the adequate management of the default, including the liquidation of the assets and positions in the account. In addition, the liquidation proceeds could not be returned readily and directly to the indirect client, for which reason they should be returned to the client for the account of its indirect clients.

- (14) Even with the gross omnibus indirect account structure, in some circumstances, the direct return of the liquidation proceeds to the indirect client cannot be conducted, such as in the case of the failure of a client providing indirect clearing services that is established in a third country where the insolvency regime would not allow the direct return of the liquidation proceeds. When the direct return of the liquidation proceeds cannot be conducted then the liquidation proceeds would need to be returned to the defaulted client for the account of the indirect clients.
- (15) Under normal circumstances, with a gross omnibus indirect account structure and process, gross margining by the CCP would mean that the assets covering the positions of one indirect client would not be exposed to losses connected to positions of another indirect client. However, in the case of a default if the positions need to be liquidated, then the risk exists of some exposure to the losses of another indirect client as the positions and collateral are comingled in one account. Yet, when positions need to be liquidated, the speed with which these positions can be liquidated can contribute to minimising the loss on the liquidation of these positions and collateral, which can be the case with the gross omnibus indirect account. In addition, under a gross margining methodology it is less likely that the positions are under collateralised, and therefore the chances of a loss are greatly minimised.
- (16) A client providing indirect clearing services should present the indirect client with a choice of account structures in accordance with this Regulation and make reasonable efforts to receive instructions from the indirect client on its choice of account and segregation model. However, in order to ensure this Regulation is complied with while ensuring a continuity of service, when the indirect client has not instructed the client of its choice of account structure within a reasonable period of time, the client should be able to provide indirect

clearing services to this indirect client using an account in accordance with this Regulation, including the account corresponding to the account choice with the minimum segregation requirement, provided that the client informs the indirect client accordingly of the use of this account, the risks of this account segregation and of the option to change account segregation at a later stage.

- (17) As indirect clearing arrangements may give rise to specific risks, all the parties participating in indirect clearing arrangements, including clearing members and CCPs, should routinely identify, monitor and manage any material risks arising from the arrangement. Appropriate sharing of information between clients that provide indirect clearing services and clearing members that facilitate those services is especially important in this context. Clearing members should use information provided by clients for risk management and margining purposes only and should prevent the misuse of commercially sensitive information, including through the use of effective barriers between different divisions of a financial institution to avoid conflicts of interest. Clearing members that offer to facilitate indirect clearing services would need to include information in relation to the levels of segregation available to clients that provide indirect clearing services, when complying with the obligation of Regulation (EU) No 648/2012 to publicly disclose the levels of protections and the costs associated with the different levels of segregation that they provide.
- (18) In many circumstances, the more intermediate entities are involved in a clearing arrangement, the higher the chances counterparty credit risk would be increased. As a result, the number of intermediate entities involved in indirect clearing arrangements should be limited. Indirect clearing arrangements introduce a new layer of intermediation compared to client clearing arrangements, thus these arrangements should typically involve four entities: the CCP, the clearing member, the client and the indirect client.

However, in order to facilitate access to CCP clearing, some groups that offer clearing services involve two entities from their group, resulting in arrangements with more intermediate entities and creating long chains. This is the case of groups that have various entities being clearing members at different CCPs but that may consolidate the offering of their clearing services in one single entity, which is the entity facing their clients. This can also be the case of a client providing indirect clearing services. For similar reasons to the group of the clearing member, the group of the client can sometimes involve one entity that faces the clearing member and another entity that faces the indirect client, typically because this second entity is established in the jurisdiction of the indirect client and it is the entity with the commercial relationship with the indirect client. In these cases, the choice of involving multiple entities is not to make the clearing arrangement more complex and with more intermediate entities, but rather to rationalise the clearing services across the activities and to simplify the commercial relationship between clearing members, clients and indirect clients.

Provided these types of arrangements, that involve two entities from the same group, and thus the involvement of more entities in indirect clearing arrangements, meet specific conditions that ensure that counterparty risk is not increased and that an appropriate level of protection is provided to the indirect clearing, they contribute to the ability for a wide range of counterparties to access various derivative markets. Typically, the counterparties that rely the most on these arrangements are usually small financial counterparties and non-financial counterparties that are less sophisticated and have less reasons or means to become a direct member or a client than the bigger counterparties.

Limiting long chains to arrangements including the basic omnibus indirect account in accordance with this Regulation would ensure counterparty risk is not increased, as the indirect clients that have chosen this type of account have chosen less segregation and less distinction from the positions and assets of the other indirect clients. The protections provided by these arrangements against a default would remain the same in the case of arrangements with two entities from the group of the clearing member and/or the group of the client.

With long chains involving two entities from the group of the clearing member and/or the group of the client, the responsibilities typically associated to clearing members, in particular the management of the default of its client, are also responsibilities that intermediate entities have with regard to the entities after them in the indirect clearing chain, thus in their case the responsibility to manage the default of their client that provides clearing services to other clients of its own. Similarly, the responsibilities typically associated to clients providing clearing services to an indirect client, in particular ensuring that the choice of accounts and segregation levels along with the associated risks are explained to the indirect client so the latter can choose the most appropriate arrangement, are also responsibilities that intermediate entities have with regard to their client, so that, in fine, in these long chains, the indirect client is provided with the same level of clearing service and level of protection.

- (19) In the scope of the mandate granted by article 30 of MiFIR, ESMA has performed a public consultation related to the development of draft regulatory technical standards related to indirect clearing for exchange traded derivatives that shall be consistent with the RTS related to indirect clearing for OTC derivatives. In view of issues raised by stakeholders, Commission Delegated Regulation (EU) No 149/2013 should be amended in order to address some of these issues. In addition, the date on which this Regulation takes effect for CCPs, clearing members, clients and indirect clients involved in indirect clearing arrangements should take into account the fact that they might need to implement some changes in their operational and legal set-up in order to comply with the amendments introduced in this Regulation.

(20) This Regulation is based on the draft regulatory technical standards submitted by the European Supervisory Authority (European Securities and Markets Authority) to the Commission.

(21) The European Supervisory Authority (European Securities and Markets Authority) has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council⁷.

HAS ADOPTED THIS REGULATION:

Article 1

Amendment to Commission Delegated Regulation (EU) No 149/2013

Commission Delegated Regulation (EU) No 149/2013 is amended as follows:

(1) Article 2 is replaced by the following:

“1. A client of a clearing member prepared to facilitate indirect clearing services shall be permitted to provide such services to one or more of its own clients, provided that it is an authorised credit institution, investment firm or an equivalent third country credit institution or investment firm, and meets the requirements referred to in Article 4(1).

2. The client of the clearing member and the indirect client shall agree upon the contractual terms of an indirect clearing arrangement, after consultation with the clearing member on the aspects that can impact the operations of the latter.

3. The contractual terms shall require the client to honour all obligations of the indirect client towards the clearing member with regards to transactions arising from the indirect clearing arrangement, and shall clearly document the scope of such arrangement.”

(2) Article 3 is replaced by the following:

“1. Indirect clearing arrangements shall not be subject to business practices of the CCP which act as a barrier to their establishment on reasonable commercial terms. At the request of

⁷ Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

a clearing member, the CCP shall open and maintain any of the accounts referred to in Article 4(4).

2. Where the assets and positions of several indirect clients are managed by the CCP in a single account provided for in Article 4(4)(b) the CCP shall keep separate records of the positions of each indirect client, calculate the margins in respect of each indirect client and collect the sum on a gross basis, based on the information referred to in Article 4(3).

3. A CCP shall identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the CCP to adverse market developments.”

(3) Article 4 is replaced by the following:

“1. A clearing member that offers to facilitate indirect clearing services shall do so on reasonable commercial terms. Without prejudice to the confidentiality of contractual arrangements with individual clients, the clearing member shall publicly disclose the general terms on which it is prepared to facilitate indirect clearing services. These terms shall include minimum financial resources and operational capacity requirements for clients that provide indirect clearing services.”

2. At the level of the clearing member, a clearing member that offers to facilitate indirect clearing services shall open and maintain at least the following accounts as indicated by the client:

- (a) an omnibus account with the assets and positions of the client held for the accounts of its indirect clients;
- (b) an omnibus account with the assets and positions of the client held for the accounts of its indirect clients, where the clearing member shall ensure that the positions of an indirect client do not offset the positions of another indirect client, and that the assets held for the account of an indirect client cannot be used to cover the positions of another indirect client.

3. When the assets and positions of several indirect clients are managed by the clearing member in a single account provided for in paragraph 2(b), the clearing member shall ensure that the CCP has all the necessary information to identify the positions held for the account of each indirect client on a daily basis. This information shall be based on the information referred to in Article 5(4).

4. At the level of the CCP, a clearing member that offers to facilitate indirect clearing services shall open and maintain the following accounts as indicated by the client:

- (a) a segregated account for the exclusive purpose of holding the assets and positions of the clearing member's indirect clients that are managed by the clearing member in an account provided for in paragraph 2(a);
 - (b) a segregated account for the exclusive purpose of holding the assets and positions of the indirect clients of each client of the clearing member that are managed by the clearing member in an account provided for in paragraph 2(b).
5. A clearing member shall establish robust procedures to manage the default of a client that provides indirect clearing services.
6. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in paragraph 2(a):
- (a) the clearing member shall ensure that the procedures referred to in paragraph 5 allow the prompt liquidation of the assets and positions of indirect clients following the default of a client, which shall include liquidating the positions of the indirect clients at the level of the CCP. The clearing member shall include in the procedures the details of the communication from the clearing member to the indirect clients, regarding the default of the client and the period of time during which the portfolios of the indirect clients will be liquidated;
 - (b) after the completion of the default management process for the default of a client, the clearing member shall readily return to the client for the account of the indirect clients any balance owed from the liquidation of the assets and positions of the indirect clients by the clearing member.
7. When the assets and positions of one or more indirect clients are managed by the client in an account provided for in paragraph 2(b):
- (a) the clearing member shall include in the procedures referred to in paragraph 5:
 - (i) the steps to conduct a transfer of the assets and positions held by the defaulting client for the account of its indirect clients to another client or to a clearing member; and
 - (ii) the steps required to initiate the payment of the proceeds from a liquidation of the assets and positions of indirect clients to each of these indirect clients;
 - (b) the clearing member shall, at least, contractually commit itself to trigger the procedures for the transfer of the assets and positions held by the defaulting client for the account of its indirect clients to another client or clearing member designated by all the indirect clients whose assets and positions are being transferred, on the relevant indirect clients' request and without the consent of the defaulting client. That other

client or clearing member shall be obliged to accept those assets and positions only where it has previously entered into a contractual relationship with the relevant indirect clients by which it has committed itself to do so;

- (c) the clearing member shall ensure that the procedures allow the prompt liquidation of the assets and positions of indirect clients following the default of the client, which shall include liquidating the positions of the indirect clients at the level of the CCP, in case the transfer to that other client or clearing member has not taken place for any reason within a predefined transfer period specified in the indirect clearing arrangements. The clearing member shall include in the procedures the details of the communication from the clearing member to the indirect clients regarding the default of the client and the period of time during which the relevant indirect client portfolios will be liquidated;
- (d) following the liquidation of the assets and positions of the indirect clients, a clearing member shall, at least, contractually commit itself to trigger the procedures for the payment of the liquidation proceeds to each of the indirect clients;
- (e) after the completion of the default management process for the default of a client, and when the clearing member has not been able to identify the indirect clients or to complete the payment of the liquidation proceeds to each of the indirect clients, the clearing member shall readily return to the client for the account of the indirect clients any balance owed from the liquidation of the assets and positions of the indirect clients by the clearing member.

8. A clearing member shall identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the clearing member to adverse market developments. The clearing member shall establish robust internal procedures to ensure the information provided by clients under Article 5(9) cannot be used for commercial purposes.”

(4) Article 5 is replaced by the following:

“1. A client that provides indirect clearing services shall offer indirect clients a choice between the accounts provided for in Article 4(2) and shall ensure that indirect clients are fully informed of the risks associated with each choice of account.

2. Where an indirect client does not reply to a request of the client to disclose its choice of account segregation within a reasonable deadline fixed by the latter, the client shall use an account provided for in Article 4(2). The client should without undue delay inform the indirect client accordingly and provide the indirect client with information on the risks associated with this level of account segregation. The indirect client can choose a different level of segregation at any time by communicating it in writing to the client.

3. A client that provides indirect clearing services shall keep separate records and accounts that enable it to distinguish between its own assets and positions and those held for the account of its indirect clients.
4. When the assets and positions of several indirect clients are managed by the clearing member in a single account provided for in Article 4(2)(b), the client shall ensure that the clearing member has all the necessary information to identify the positions held for the account of each indirect client on a daily basis.
5. A client that provides indirect clearing services shall request the clearing member to open and maintain at the level of the CCP the accounts referred to in Article 4(4) corresponding to the choice of the indirect clients in accordance with paragraph 1.
6. A client that provides indirect clearing services shall disclose to its clients the details of the different levels of segregation and a description of the risks involved with the respective levels of segregation offered.
7. A client shall provide the indirect client with sufficient information to identify the CCP and the clearing member used to clear the indirect client's positions.
8. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in Article 4(2)(b), the client that provides indirect clearing services shall include, in its contractual arrangement with indirect clients, terms to facilitate the prompt return by the clearing member to the indirect client of the proceeds from the liquidation of the positions and assets held for the account of the indirect client in case of default of the client.
9. A client shall provide the clearing member with sufficient information to identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the clearing member.
10. The client shall have arrangements in place ensuring that, in the event of default of the client, all information held by the client in respect of its indirect clients is made immediately available to the clearing member."

(5) Article 5b is added:

"Article 5b

Long chains

1. By way of derogation to Article 1, "indirect client" shall mean the client of an indirect client ("end indirect client"), and accordingly, "indirect clearing arrangement" shall mean the set of contractual relationships between a central counterparty, a clearing member, the

client of a clearing member, an indirect client and the client of an indirect client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:

- (a) the indirect client that provides clearing services is an authorised credit institution, investment firm or equivalent third country credit institution or investment firm;
 - (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a); and
 - (c) the clearing member and the client of the clearing member are part of the same group, but the indirect client is not part of that group.
2. By way of derogation to Article 1, “indirect client” shall mean the client of an indirect client (“end indirect client”), and accordingly, “indirect clearing arrangement” shall mean the set of contractual relationships between a central counterparty, a clearing member, the client of a clearing member, an indirect client and the client of an indirect client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:
- (a) the indirect client that provides clearing services is an authorised credit institution, investment firm or equivalent third country credit institution or investment firm;
 - (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a); and
 - (c) the client of the clearing member and the indirect client are part of the same group, but neither the clearing member nor the end indirect client are part of that group.
3. By way of derogation to Article 1, “indirect client” shall mean the client of a client of an indirect client (“end indirect client”), and accordingly, “indirect clearing arrangement” shall mean the set of contractual relationships between a central counterparty, a clearing member, the client of a clearing member, an indirect client, the client of an indirect client and its client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:
- (a) the indirect client and its client are authorised credit institutions, investment firms or equivalent third country credit institutions or investment firms;

- (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a);
 - (c) the clearing member and the client of the clearing member are part of the same group, but the indirect client is not part of that group; and
 - (d) the indirect client and its client are part of the same group, but the end indirect client is not part of that group.
4. Where transactions are cleared through the arrangement referred to in paragraph 1:
- (a) Articles 4(1), 4(5), 4(6) and 4(8) apply also to the client of the clearing member as if it were a clearing member; and
 - (b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to the indirect client providing clearing services as if it were a client of the clearing member.
5. Where transactions are cleared through the arrangement referred to in paragraph 2:
- (a) Articles 4(5) and 4(6) apply also to the client of the clearing member as if it were a clearing member; and
 - (b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to the indirect client providing clearing services as if it were a client of the clearing member.
6. Where transactions are cleared through the arrangement referred to in paragraph 3:
- (a) Articles 4(1), 4(5), 4(6) and 4(8) apply also to both the client of the clearing member and to its client as if they were clearing members; and
 - (b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to both the client of the clearing member and its client that are both providing clearing services as if they were clients of a clearing member.
7. The Articles referred to in paragraphs 4, 5 and 6 apply *mutatis mutandis* to the concerned entities.”

Article 2

Entry into force



This Regulation shall enter into force two months following that of its publication in the Official Journal of the European Union.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

*For the Commission
The President*

*[For the Commission
On behalf of the President*

[Position

3.3.2 Draft RTS on the indirect clearing arrangements under MiFIR

COMMISSION DELEGATED REGULATION (EU) No .../..

of **XXX**

[...]

**supplementing Regulation (EU) No 600/2014 of the European Parliament and the Council
with regard to regulatory technical standards on indirect clearing arrangements
of []
(text with EEA relevance)**

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments, and in particular Article 30 thereof,

Whereas:

- (1) An indirect clearing arrangement should not expose a CCP, clearing member, client or indirect client to additional counterparty risk and the assets and positions of the indirect client should benefit from an appropriate level of protection. It is therefore essential that any type of indirect clearing arrangements comply with minimum conditions for ensuring their safety. To that end, the parties involved in indirect clearing arrangements should be subject to specific obligations and indirect clearing arrangements should only be permissible provided that they meet the conditions defined in this Regulation. Such arrangements extend beyond the contractual relationship between indirect clients and the client of a clearing member that provides indirect clearing services.
- (2) As the assets and positions of the counterparty in indirect clearing arrangements must benefit from protection with equivalent effect to that referred to in Articles 39 and 48 of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories⁸, the concept of indirect client, stemming from that Regulation but not defined therein, is pivotal for this Regulation and should be defined herein.
- (3) Regulation (EU) No 648/2012 requires a CCP to be a designated system under Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement

⁸ OJ L 201, 27.7.2012, p.1.

finality in payment and securities settlement systems⁹. This implies that clearing members of CCPs should qualify as participants within the meaning of that Directive. Therefore, to ensure an equivalent level of protection to indirect clients as granted to clients under Regulation (EU) No 648/2012, it is necessary to ensure that clients providing indirect clearing services are credit institutions, investment firms, or equivalent third country credit institutions or investment firms.

- (4) Indirect clearing arrangements involve by design a larger number of entities in comparison to direct clearing arrangements. The larger number of intermediate entities in indirect clearing arrangements means there is a higher degree of intermediation activity between the CCP and the indirect client. Additional intermediate entities and the resulting increased intermediation activity require additional operational steps, additional accounts as well as more complex technological solutions and processing flows. The increased complexity associated to the higher number of entities between the CCP and the indirect client compared to client clearing arrangements should be mitigated with requirements for an alternative and operationally simpler choice of account structures for indirect clearing arrangements than for client clearing arrangements.
- (5) For client clearing, Regulation (EU) No 648/2012 specifies two account structures. The first account structure is an omnibus account. This account structure is the less complex structure that can be required while still ensuring a separation between the collateral and positions of the indirect client and the collateral and positions of the client providing clearing services. The requirement for this first account structure should therefore be mirrored for indirect clearing arrangements.
- (6) The second account structure is an individually segregated account, which requires separate accounts for each client and thus an increased number of operational processes to manage all the separate accounts than if the clients were managed in a single account. Requiring such an account structure in the case of indirect clearing services would multiply the number of necessary accounts and related operational processes, raising the complexity, cost and operational risk of indirect clearing arrangements.
- (7) Alternatively, a gross omnibus indirect account structure with a mechanism of a transfer of margin from the indirect client all the way to the CCP would allow to achieve an equivalent distinction between the collateral and the positions held for the account of a specific indirect client from the collateral and the positions held for the account of the direct client or other indirect clients, while requiring a much simpler account structure. Such an alternative account structure and processing would reduce the number of accounts to be opened and maintained and therefore the related number of operational steps to margin and settle collateral in these accounts. This structure would reduce the cost and

⁹ OJ L 166, 11.6.1998, p. 45.

complexity compared to individually segregated accounts, while still permitting to distinguish the collateral and the positions of different indirect clients and therefore ensuring an equivalent level of protection as an individually segregated account. Although this would not preclude individually segregated indirect accounts to also be offered.

- (8) In order to ensure that the same amount of margin would be called with a gross omnibus indirect account structure as if the indirect client were using an individually segregated indirect clearing account structure, the CCP would need information on the positions held for the account of the indirect client in order to calculate the associated margin call on an indirect client by indirect client basis.
- (9) Margining on a gross basis would imply that the netting of positions of different indirect clients in the same gross omnibus indirect account, or the use of the margin of an indirect client to cover for the margin requirement of another indirect client in the same gross omnibus account, could not be performed when recording the positions of each indirect client and when calculating and calling the corresponding margin requirements.
- (10) Margins are the first line of defence in case of a default and maintaining margins at the level of the CCP protects the clients from the default of the clearing member. Requiring passing margins all the way to the CCP would protect the indirect client not only from the default of a client, but also from the default of the clearing member.
- (11) Any additional collateral received above the margin amount called by the clearing member should be treated in accordance with the relevant terms of the indirect clearing arrangements.
- (12) As for client clearing, where, following the failure of a clearing member that facilitates clearing services, the CCP should be prepared to transfer the clients positions to an alternative clearing member and to liquidate them if necessary, for indirect clearing, the clearing member should have procedures to facilitate the transfer of indirect clients' positions to an alternative client following the failure of a client that facilitates indirect clearing services. The clearing member should also have procedures to liquidate the positions and assets of the indirect clients and to return the liquidation proceeds to the indirect clients when known. And when the client that fails has been facilitating clearing services with a gross omnibus indirect account structure, the clearing member should commit to trigger these procedures.
- (13) Under the gross omnibus indirect account structure, the information on the positions held for the account of each indirect client is passed daily to the different entities involved in the indirect clearing arrangement without the exact identity of the indirect clients. Therefore, safeguards should be put in place so that in the case of the default of the client, the information on the identity of the indirect clients can become known to the clearing

member so that the identification of which assets and positions belong to which indirect client can be done.

However, this is not the case with the other choice of account structure, the basic omnibus indirect account structure, the information on the positions held for the account of each indirect client is not passed on, so in the case of the default of the client, the identification of which assets and positions belong to which indirect client might not be unequivocally and quickly determined. In such a situation porting would be unrealistic and the time taken to attempt porting would introduce delays and risk to the adequate management of the default, including the liquidation of the assets and positions in the account. In addition, the liquidation proceeds could not be returned readily and directly to the indirect client, for which reason they should be returned to the client for the account of its indirect clients.

- (14) Even with the gross omnibus indirect account structure, in some circumstances, the direct return of the liquidation proceeds to the indirect client cannot be conducted, such as in the case of the failure of a client providing indirect clearing services that is established in a third country where the insolvency regime would not allow the direct return of the liquidation proceeds. When the direct return of the liquidation proceeds cannot be conducted then the liquidation proceeds would need to be returned to the defaulted client for the account of the indirect clients.
- (15) Under normal circumstances, with a gross omnibus indirect account structure and process, gross margining by the CCP would mean that the assets covering the positions of one indirect client would not be exposed to losses connected to positions of another indirect client. However, in the case of a default if the positions need to be liquidated, then the risk exists of some exposure to the losses of another indirect client as the positions and collateral are comingled in one account. Yet, when positions need to be liquidated, the speed with which these positions can be liquidated can contribute to minimising the loss on the liquidation of these positions and collateral, which can be the case with the gross omnibus indirect account.
- (16) A client providing indirect clearing services should present the indirect client with a choice of account structures in accordance with this Regulation and make reasonable efforts to receive instructions from the indirect client on its choice of account and segregation model. However, in order to ensure this Regulation is complied with while ensuring a continuity of service, when the indirect client has not instructed the client of its choice of account structure within a reasonable period of time, the client should be able to provide indirect clearing services to this indirect client using an account in accordance with this Regulation, including the account corresponding to the account choice with the minimum segregation requirement, provided that the client informs the indirect client accordingly of the use of this account, the risks of this account segregation and of the option to change account segregation at a later stage.

(17) As indirect clearing arrangements may give rise to specific risks, all the parties participating in indirect clearing arrangements, including clearing members and CCPs, should routinely identify, monitor and manage any material risks arising from the arrangement. Appropriate sharing of information between clients that provide indirect clearing services and clearing members that facilitate those services is especially important in this context. Clearing members should use information provided by clients for risk management and margining purposes only and should prevent the misuse of commercially sensitive information, including through the use of effective barriers between different divisions of a financial institution to avoid conflicts of interest. Clearing members that offer to facilitate indirect clearing services would need to include information in relation to the levels of segregation available to clients that provide indirect clearing services, when complying with the obligation of Regulation (EU) No 648/2012 to publicly disclose the levels of protections and the costs associated with the different levels of segregation that they provide.

(18) In many circumstances, the more intermediate entities are involved in a clearing arrangement, the higher the chances counterparty credit risk would be increased. As a result, the number of intermediate entities involved in indirect clearing arrangements should be limited. Indirect clearing arrangements introduce a new layer of intermediation compared to client clearing arrangements, thus these arrangements should typically involve four entities: the CCP, the clearing member, the client and the indirect client.

However, in order to facilitate access to CCP clearing, some groups that offer clearing services involve two entities from their group, resulting in arrangements with more intermediate entities and creating long chains. This is the case of groups that have various entities being clearing members at different CCPs but that may consolidate the offering of their clearing services in one single entity, which is the entity facing their clients. This can also be the case of a client providing indirect clearing services. For similar reasons to the group of the clearing member, the group of the client can sometimes involve one entity that faces the clearing member and another entity that faces the indirect client, typically because this second entity is established in the jurisdiction of the indirect client and it is the entity with the commercial relationship with the indirect client. In these cases, the choice of involving multiple entities is not to make the clearing arrangement more complex and with more intermediate entities, but rather to rationalise the clearing services across the activities and to simplify the commercial relationship between clearing members, clients and indirect clients.

Provided these types of arrangements, that involve two entities from the same group, and thus the involvement of more entities in indirect clearing arrangements, meet specific conditions that ensure that counterparty risk is not increased and that an appropriate level of protection is provided to the indirect clearing, they contribute to the ability for a wide range of counterparties to access various derivative markets. Typically, the counterparties

that rely the most on these arrangements are usually small financial counterparties and non-financial counterparties that are less sophisticated and have less reasons or means to become a direct member or a client than the bigger counterparties.

Limiting long chains to arrangements including the basic omnibus indirect account in accordance with this Regulation would ensure counterparty risk is not increased, as the indirect clients that have chosen this type of account have chosen less segregation and less distinction from the positions and assets of the other indirect clients. The protections provided by these arrangements against a default would remain the same in the case of arrangements with two entities from the group of the clearing member and/or the group of the client.

With long chains involving two entities from the group of the clearing member and/or the group of the client, the responsibilities typically associated to clearing members, in particular the management of the default of its client, are also responsibilities that intermediate entities have with regard to the entities after them in the indirect clearing chain, thus in their case the responsibility to manage the default of their client that provides clearing services to other clients of its own. Similarly, the responsibilities typically associated to clients providing clearing services to an indirect client, in particular ensuring that the choice of accounts and segregation levels along with the associated risks are explained to the indirect client so the latter can choose the most appropriate arrangement, are also responsibilities that intermediate entities have with regard to their client, so that, in fine, in these long chains, the indirect client is provided with the same level of clearing service and level of protection.

(19) This Regulation is based on the draft regulatory technical standards submitted by the European Supervisory Authority (European Securities and Markets Authority) to the Commission.

(20) The European Supervisory Authority (European Securities and Markets Authority) has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council¹⁰.

HAS ADOPTED THIS REGULATION:

¹⁰ Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

Article 1

Definitions

For the purposes of this Regulation the following definitions apply:

- (1) “client” means a client as defined in Article 2(15) of Regulation (EU) No 648/2012;
- (2) “indirect client” means an indirect client as defined in Article 1(a) of Commission Delegated Regulation (EU) No 149/2013;
- (3) “indirect clearing arrangement” or “indirect clearing service arrangement” means an indirect clearing arrangement or an indirect clearing service arrangement as defined in Article 1(b) of Commission Delegated Regulation (EU) No 149/2013.

Article 2

Structure of indirect clearing arrangements

1. A client of a clearing member prepared to facilitate indirect clearing services shall be permitted to provide such services to one or more of its own clients, provided that it is an authorised credit institution, investment firm or an equivalent third country credit institution or investment firm, and meets the requirements referred to in Article 4(1).
2. The client of the clearing member and the indirect client shall agree upon the contractual terms of an indirect clearing arrangement, after consultation with the clearing member on the aspects that can impact the operations of the latter.
3. The contractual terms shall require the client to honour all obligations of the indirect client towards the clearing member with regards to transactions arising from the indirect clearing arrangement, and shall clearly document the scope of such arrangement.

Article 3

Obligations of CCPs

1. Indirect clearing arrangements shall not be subject to business practices of the CCP which act as a barrier to their establishment on reasonable commercial terms. At the request of a clearing member, the CCP shall open and maintain any of the accounts referred to in Article 4(4).

2. Where the assets and positions of several indirect clients are managed by the CCP in a single account provided for in Article 4(4)(b), the CCP shall keep separate records of the positions of each indirect client, calculate the margins in respect of each indirect client and collect the sum on a gross basis, based on the information referred to in Article 4(3).

3. A CCP shall identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the CCP to adverse market developments.

Article 4

Obligations of clearing members

1. A clearing member that offers to facilitate indirect clearing services shall do so on reasonable commercial terms. Without prejudice to the confidentiality of contractual arrangements with individual clients, the clearing member shall publicly disclose the general terms on which it is prepared to facilitate indirect clearing services. These terms shall include minimum financial resources and operational capacity requirements for clients that provide indirect clearing services.

2. At the level of the clearing member, a clearing member that offers to facilitate indirect clearing services shall open and maintain at least the following accounts as indicated by the client:

- (a) an omnibus account with the assets and positions of the client held for the accounts of its indirect clients;
- (b) an omnibus account with the assets and positions of the client held for the accounts of its indirect clients, where the clearing member shall ensure that the positions of an indirect client do not offset the positions of another indirect client, and that the assets held for the account of an indirect client cannot be used to cover the positions of another indirect.

3. When the assets and positions of several indirect clients are managed by the clearing member in a single account provided for in paragraph 2(b), the clearing member shall ensure that the CCP has all the necessary information to identify the positions held for the account of each indirect client on a daily basis. This information shall be based on the information referred to in Article 5(4).

4. At the level of the CCP, a clearing member that offers to facilitate indirect clearing services shall open and maintain the following accounts as indicated by the client:

- (a) a segregated account for the exclusive purpose of holding the assets and positions of the clearing member's indirect clients that are managed by the clearing member in an account provided for in paragraph 2(a);
 - (b) a segregated account for the exclusive purpose of holding the assets and positions of the indirect clients of each client of the clearing member that are managed by the clearing member in an account provided for in paragraph 2(b).
5. A clearing member shall establish robust procedures to manage the default of a client that provides indirect clearing services.
6. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in paragraph 2(a):
- (a) the clearing member shall ensure that the procedures referred to in paragraph 5 allow the prompt liquidation of the assets and positions of indirect clients following the default of a client, which shall include liquidating the positions of the indirect clients at the level of the CCP. The clearing member shall include in the procedures the details of the communication from the clearing member to the indirect clients, regarding the default of the client and the period of time during which the portfolios of the indirect clients will be liquidated;
 - (b) after the completion of the default management process for the default of a client, the clearing member shall readily return to the client for the account of the indirect clients any balance owed from the liquidation of the assets and positions of the indirect clients by the clearing member.
7. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in paragraph 2(b):
- (a) the clearing member shall include in the procedures referred to in paragraph 5:
 - (i) the steps to conduct a transfer of the assets and positions held by the defaulting client for the account of its indirect clients to another client or to a clearing member; and
 - (ii) the steps required to initiate the payment of the proceeds from a liquidation of the assets and positions of indirect clients to each of these indirect clients;
 - (b) the clearing member shall, at least, contractually commit itself to trigger the procedures for the transfer of the assets and positions held by the defaulting client for the account of its indirect clients to another client or clearing member designated by all the indirect clients whose assets and positions are being transferred, on the relevant indirect clients' request and without the consent of the defaulting client. That other

client or clearing member shall be obliged to accept those assets and positions only where it has previously entered into a contractual relationship with the relevant indirect clients by which it has committed itself to do so;

- (c) the clearing member shall ensure that the procedures allow the prompt liquidation of the assets and positions of indirect clients following the default of the client, which shall include liquidating the positions of the indirect clients at the level of the CCP, in case the transfer to that other client or clearing member has not taken place for any reason within a predefined transfer period specified in the indirect clearing arrangements. The clearing member shall include in the procedures the details of the communication from the clearing member to the indirect clients regarding the default of the client and the period of time during which the relevant indirect client portfolios will be liquidated;
- (d) following the liquidation of the assets and positions of the indirect clients, the clearing member shall, at least, contractually commit itself to trigger the procedures for the payment of the liquidation proceeds to each of the indirect clients;
- (e) after the completion of the default management process for the default of a client, and when the clearing member has not been able to identify the indirect clients or to complete the payment of the liquidation proceeds to each of the indirect clients, the clearing member shall readily return to the client for the account of the indirect clients any balance owed from the liquidation of the assets and positions of the indirect clients by the clearing member.

8. A clearing member shall identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the clearing member to adverse market developments. The clearing member shall establish robust internal procedures to ensure the information provided by clients under Article 5(9) cannot be used for commercial purposes.

Article 5

Obligations of clients

1. A client that provides indirect clearing services shall offer indirect clients a choice between the accounts provided for in Article 4(2) and shall ensure that indirect clients are fully informed of the risks associated with each choice of account.

2. Where an indirect client does not reply to a request of the client to disclose its choice of account segregation within a reasonable deadline fixed by the latter, the client shall use an

account provided for in Article 4(2). The client should without undue delay inform the indirect client accordingly and provide the indirect client with information on the risks associated with this level of account segregation. The indirect client can choose a different level of segregation at any time by communicating it in writing to the client.

3. A client that provides indirect clearing services shall keep separate records and accounts that enable it to distinguish between its own assets and positions and those held for the account of its indirect clients.

4. When the assets and positions of several indirect clients are managed by the clearing member in a single account provided for in Article 4(2)(b), the client shall ensure that the clearing member has all the necessary information to identify the positions held for the account of each indirect client on a daily basis.

5. A client that provides indirect clearing services shall request the clearing member to open and maintain at the level of the CCP the accounts referred to in Article 4(4) corresponding to the choice of the indirect clients in accordance with paragraph 1.

6. A client that provides indirect clearing services shall disclose to its clients the details of the different levels of segregation and a description of the risk involved with the respective levels of segregation offered.

7. A client shall provide the indirect client with sufficient information to identify the CCP and the clearing member used to clear the indirect client's positions.

8. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in Article 4(2)(b), the client that provides indirect clearing services shall include, in its contractual arrangement with indirect clients, terms to facilitate the prompt return by the clearing member to the indirect client of the proceeds from the liquidation of the positions and assets held for the account of the indirect client in case of default of the client.

9. A client shall provide the clearing member with sufficient information to identify, monitor and manage any material risks arising from facilitating indirect clearing services that could affect the resilience of the clearing member.

10. The client shall have arrangements in place ensuring that, in the event of default of the client, all information held by the client in respect of its indirect clients is made immediately available to the clearing member.

11. When the assets and positions of one or more indirect clients are managed by the clearing member in an account provided for in Article 4(2)(b), the information referred to in

paragraph 10 shall include the details allowing to identify the indirect clients in relation to the information under paragraph 4.

Article 6

Long chains

1. By way of derogation to Article 1, “indirect client” shall mean the client of an indirect client (“end indirect client”), and accordingly, “indirect clearing arrangement” shall mean the set of contractual relationships between a central counterparty, a clearing member, the client of a clearing member, an indirect client and the client of an indirect client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:

- (a) the indirect client that provides clearing services is an authorised credit institution, investment firm or equivalent third country credit institution or investment firm;
- (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a); and
- (c) the clearing member and the client of the clearing member are part of the same group, but the indirect client is not part of that group.

2. By way of derogation to Article 1, “indirect client” shall mean the client of an indirect client (“end indirect client”), and accordingly, “indirect clearing arrangement” shall mean the set of contractual relationships between a central counterparty, a clearing member, the client of a clearing member, an indirect client and the client of an indirect client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:

- (a) the indirect client that provides clearing services is an authorised credit institution, investment firm or equivalent third country credit institution or investment firm;
- (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a); and
- (c) the client of the clearing member and the indirect client are part of the same group, but neither the clearing member nor the end indirect client are part of that group.

3. By way of derogation to Article 1, “indirect client” shall mean the client of a client of an indirect client (“end indirect client”), and accordingly, “indirect clearing arrangement” shall mean the set of contractual relationships between a central counterparty, a clearing member, the client of a clearing member, an indirect client, the client of an indirect client and its client, which arrangement allows these entities to provide clearing services to an end indirect client, when all the following conditions are met:

- (a) the indirect client and its client are authorised credit institutions, investment firms or equivalent third country credit institutions or investment firms;
- (b) the transactions arising as part of this indirect clearing arrangement are exclusively transactions entered into by the end indirect client or end indirect clients whose assets and positions are managed by the clearing member in an account provided for in Article 4(2)(a);
- (c) the clearing member and the client of the clearing member are part of the same group, but the indirect client is not part of that group; and
- (d) the indirect client and its client are part of the same group, but the end indirect client is not part of that group.

4. Where transactions are cleared through the arrangement referred to in paragraph 1:

- (a) Articles 4(1), 4(5), 4(6) and 4(8) apply also to the client of the clearing member as if it were a clearing member; and
- (b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to the indirect client providing clearing services as if it were a client of the clearing member.

5. Where transactions are cleared through the arrangement referred to in paragraph 2:

- (a) Articles 4(5) and 4(6) apply also to the client of the clearing member as if it were a clearing member; and
- (b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to the indirect client providing clearing services as if it were a client of the clearing member.

6. Where transactions are cleared through the arrangement referred to in paragraph 3:

- (a) Articles 4(1), 4(5), 4(6) and 4(8) apply also to both the client of the clearing member and to its client as if they were clearing members; and

(b) Articles 2(2), 5(2), 5(3), 5(6), 5(7), 5(9) and 5(10) apply also to both the client of the client of the clearing member and its client that are both providing clearing services as if they were clients of a clearing member.

7. The Articles referred to in paragraphs 4, 5 and 6 apply mutatis mutandis to the concerned entities.

Article 7

Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

It shall apply from 3 January 2017.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

*For the Commission
The President*

*[For the Commission
On behalf of the President*

[Position

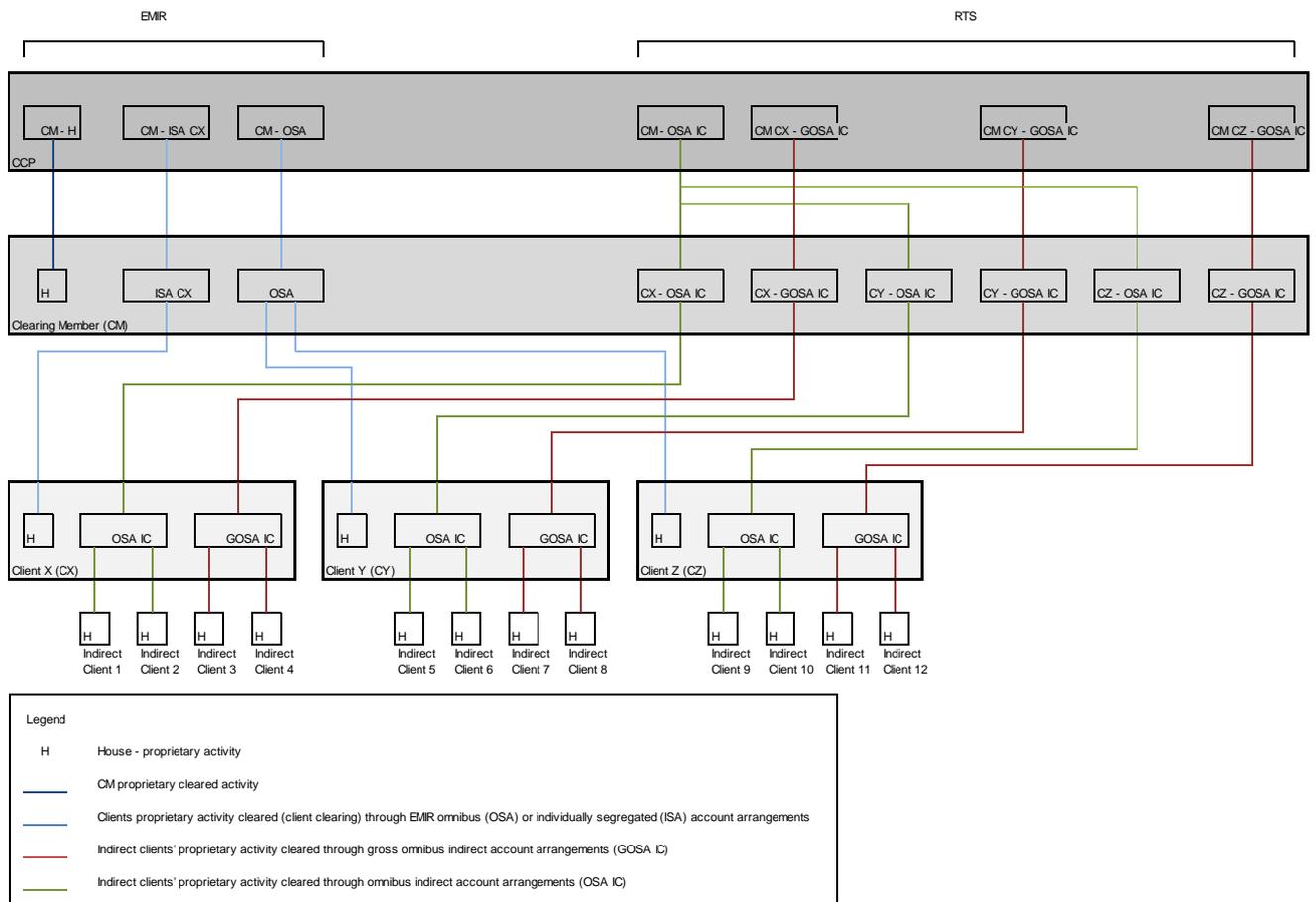
3.4 Annex IV – Diagrams of account structures

1. In this section some diagrams are presented for illustration purposes only, but do not represent any particular required set-ups. For clarity, the requirements are set in the draft RTS and the explanation on how the feedback has been integrated are developed in the first sections of this final report

3.4.1 Illustration of a full account structure

2. The below diagram represents the different accounts used to clear at a CCP the activity of a clearing member, three clients and twelve indirect clients that have made various segregation choices. Clearing as a direct member and client clearing arrangements are detailed in EMIR, whereas the indirect clearing arrangements are addressed in this final report.

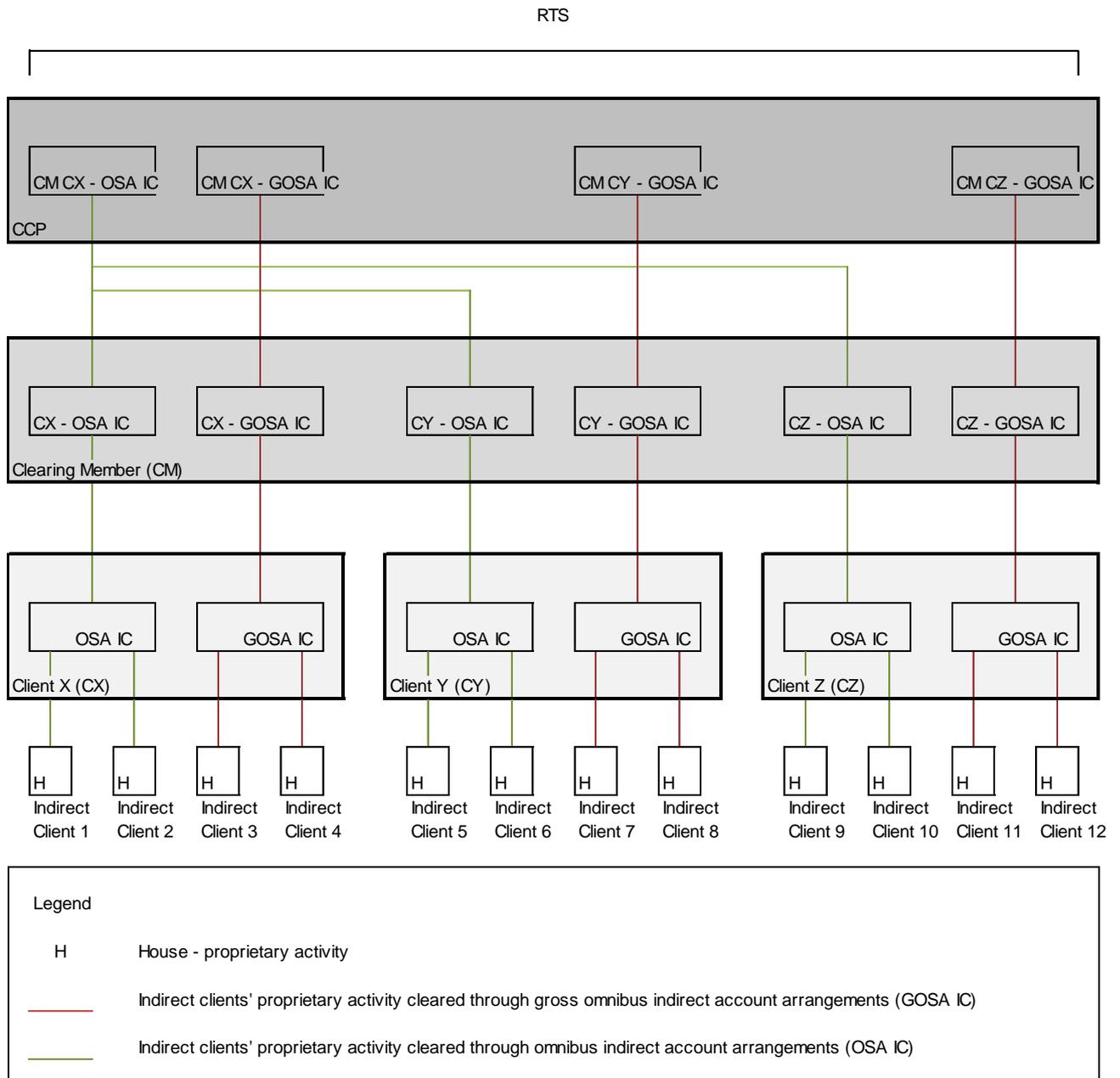
Diagram (1 OSA IC per clearing member and 1 GOSA IC per pair of clearing member/client)



3.4.2 Illustration of an account structure with respect to indirect clearing only

- The below diagram is an extract from the diagram from section 3.4.1. Specifically, it represents only the indirect clearing arrangements of the diagram from section 3.4.1, as that is the part most relevant for this final report and it also eases the reading of the diagram. The direct clearing and client clearing arrangements are not represented.

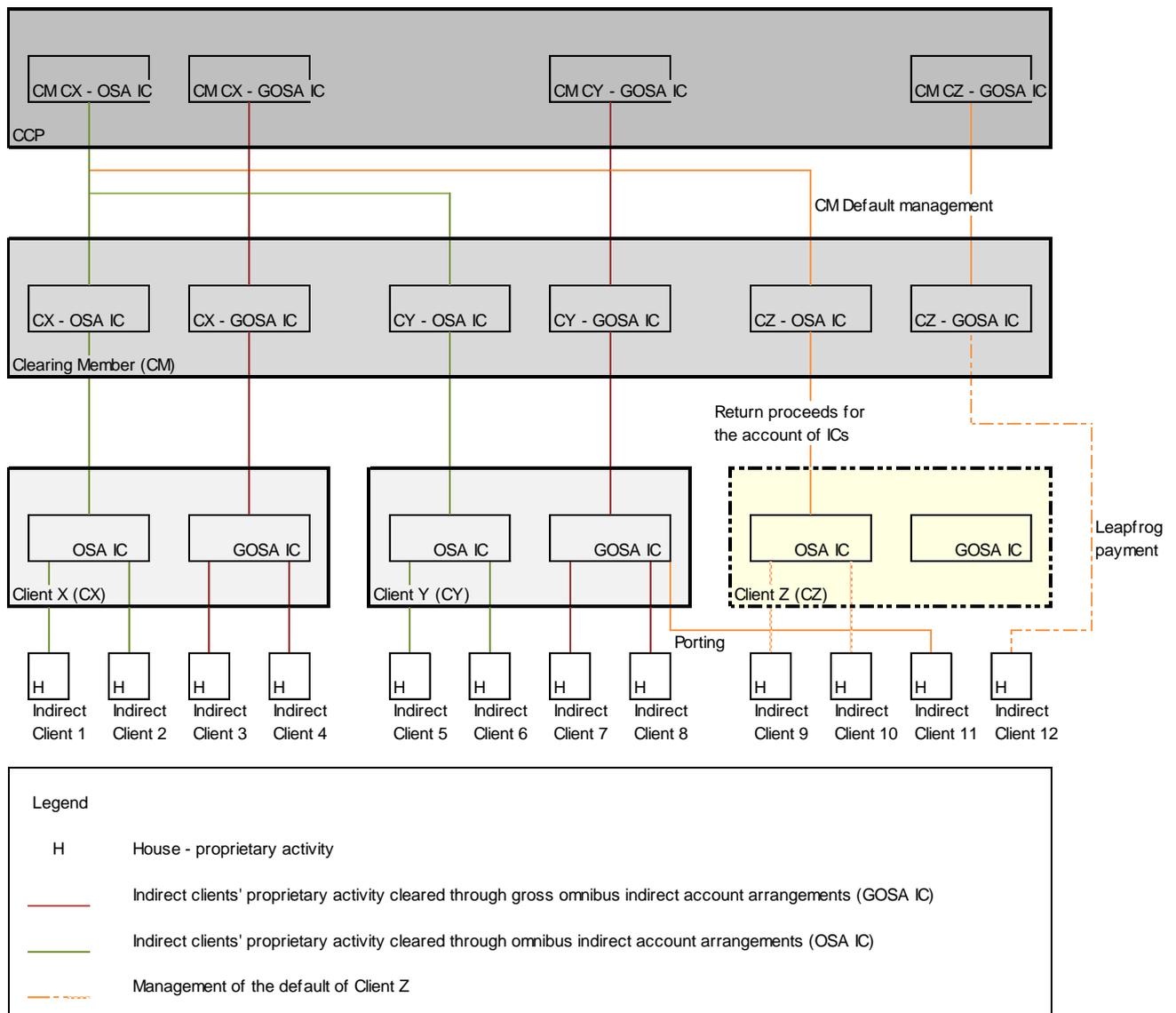
Diagram (1 OSA IC per clearing member and 1 GOSA IC per pair of clearing member/client)



3.4.3 Illustration of a default management in the context of one client providing indirect clearing services defaulting

- The below diagram represents an illustration of the management of the default of a client, Client Z from the diagram from section 3.4.2. The management of the cleared proprietary activity of Client Z is not represented.

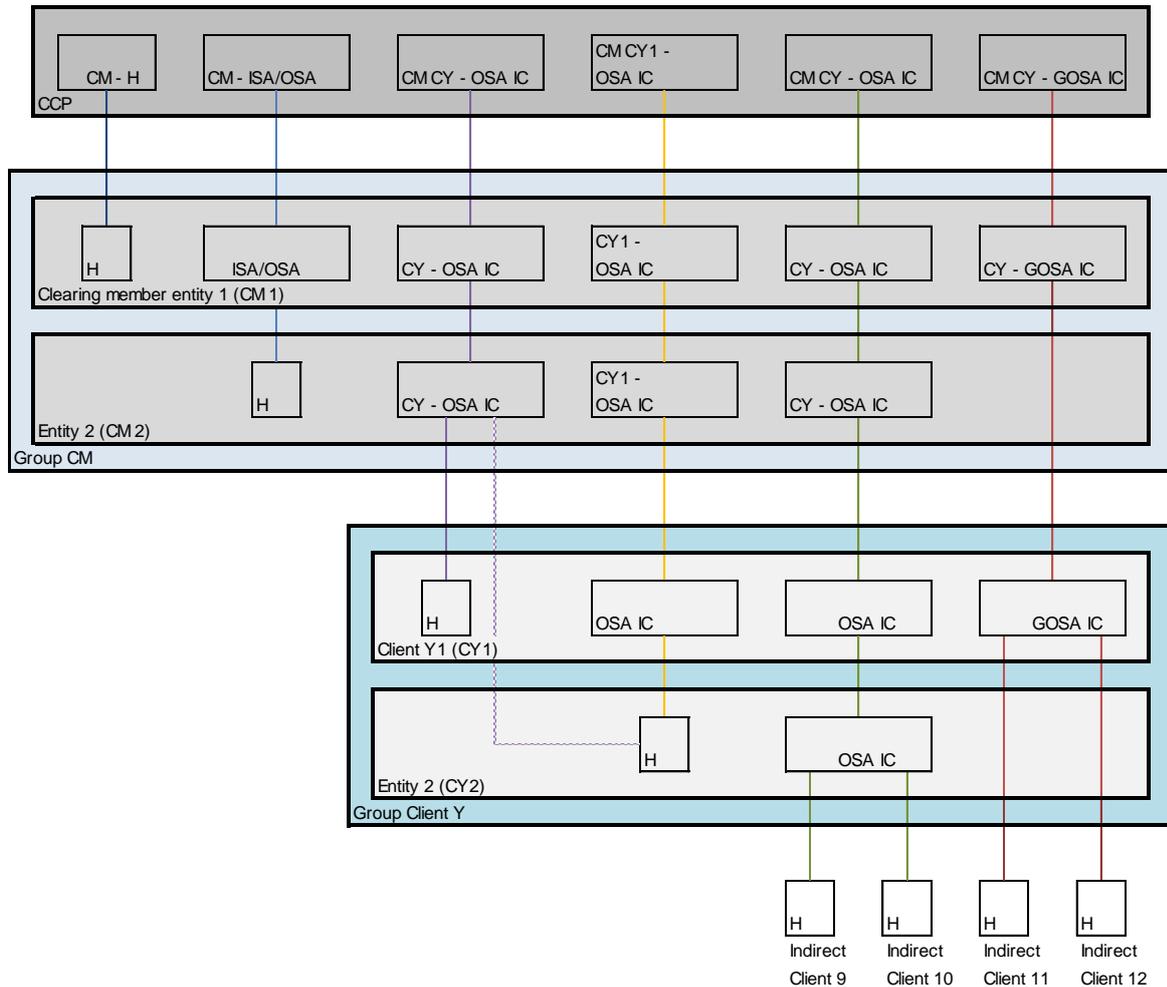
Diagram (1 OSA IC per clearing member and 1 GOSA IC per pair of clearing member/client)



3.4.4 Illustration of an account structure of long chains with successive entities from the same group

5. The below diagram displays a potential set of accounts used to clear at a CCP the activity of a clearing member, its affiliate, a client and its affiliate as well as four indirect clients that have made various segregation choices. The objective of this diagram is to illustrate the fact that the indirect clearing activity in long chains under the group approach is segregated from the other clearing activity of the involved entities, that it is limited to the basic omnibus account choice and that no more than two entities from a group can facilitate such arrangement.

Diagram of a long chain with the group approach (2 entities from the same group only and only for the OSA IC)

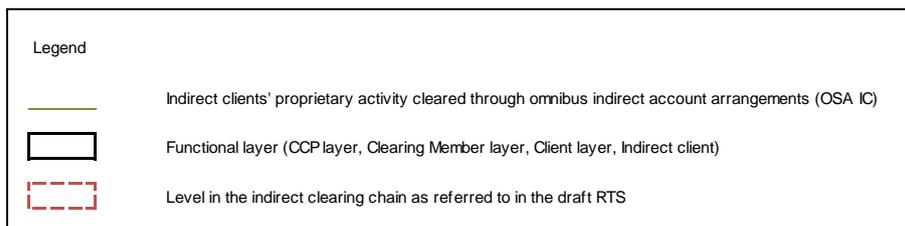
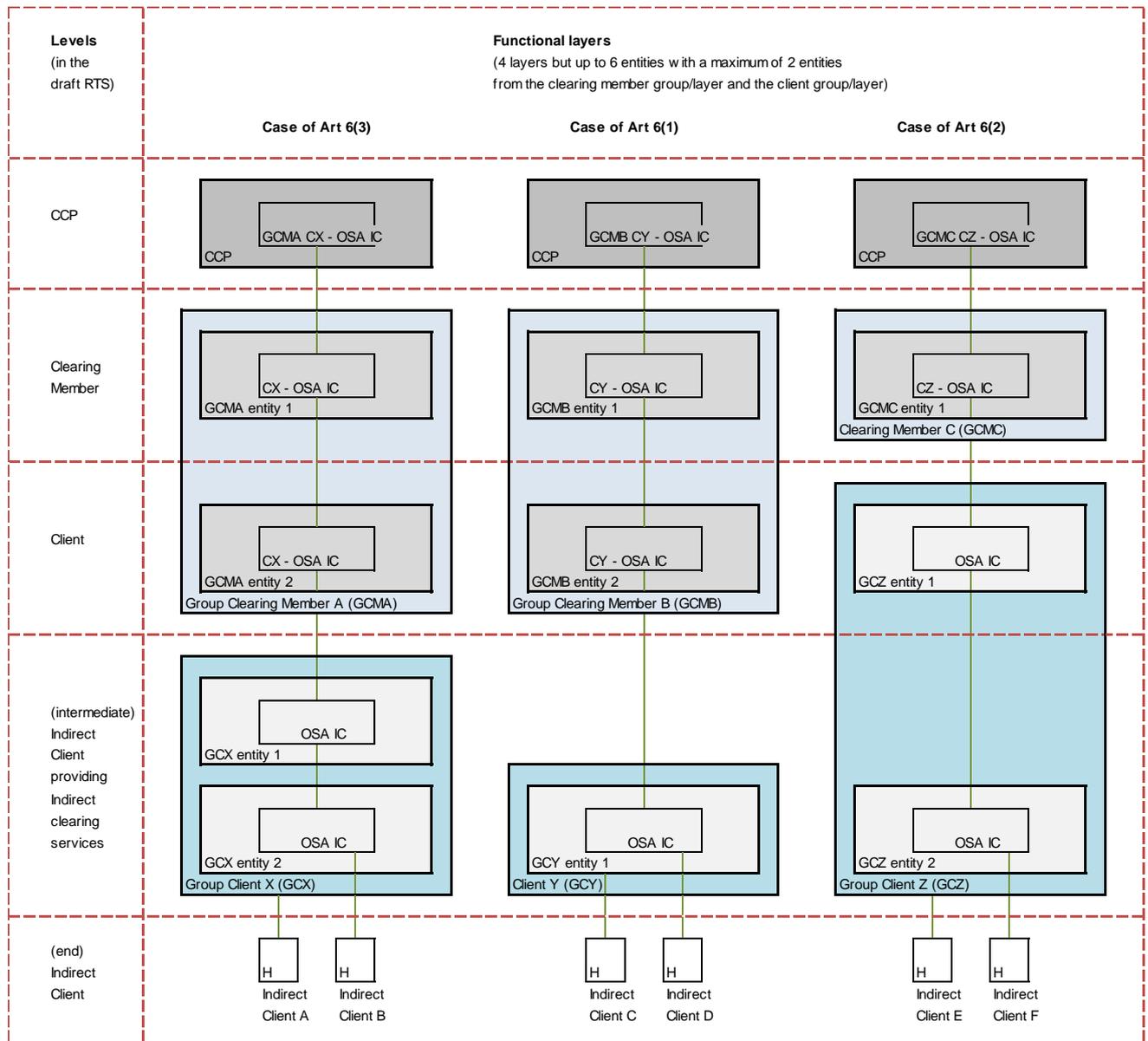


Legend	
H	House - proprietary activity
	CM1 proprietary directly cleared activity
	CM1 affiliates proprietary activity cleared (client clearing) through EMIR omnibus (OSA) or individually segregated (ISA) account arrangements
	CY1 proprietary activity cleared (client clearing) through EMIR OSA or ISA arrangements
	CY1 affiliates proprietary activity cleared (indirect clearing) through basic OSA IC or GOSA IC arrangements
	Alternative possibility for CY1 affiliates to clear their proprietary activity, in this case cleared (client clearing) through EMIR OSA or ISA arrangements
	Indirect clients' proprietary activity cleared through gross omnibus indirect account arrangements (GOSA IC)
	Indirect clients' proprietary activity cleared through omnibus indirect account arrangements (OSA IC)

6. The below diagram focuses only on the indirect clearing arrangements under the group approach and does not reflect the other clearing activity these entities can conduct respectively. The objective of this diagram is to illustrate a few sets of accounts used to clear the activity of indirect clients with long chains and with one or two intermediaries

having two entities from their group involved in the arrangement (being the clearing member and/or the client with two entities involved).

Diagram of three long chains with the group approach (with the clearing member and/or the client being in groups with 2 entities involved respectively)



7. In the arrangement to the left of the diagram, both the group of the clearing member and the group of the client have two entities involved, resulting in an indirect clearing chain that is made of what could still be considered 4 layers but with 6 entities. This is to be considered in conjunction with Article 6(3).
8. In the arrangement in the middle of the diagram, only the clearing member is in a group with two entities involved in the indirect clearing chain, resulting in a chain that is made of what could still be considered 4 layers but with 5 entities. This is to be considered in conjunction with Article 6(1).
9. Finally, to the right of the diagram, only the client is in a group with two entities involved in the indirect clearing chain, resulting in a chain that is made of what could still be considered 4 layers but with 5 entities. This is to be considered in conjunction with Article 6(2).
10. It is to be noted that the diagram also displays the difference between the functional layer and the level referred in the regulation. Indeed, a group, being the group of a clearing member or the group of a client, can have entities from the indirect clearing chain corresponding to different levels as referred to in the regulation. For example, a clearing member group could have a first entity, the one facing the CCP, falling in the clearing member definition and the entity after this first entity falling in the client definition. Similarly, a client group could have entities in the chain falling in the client and/or indirect client definitions.