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COMMISSION

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COMMISSION IMPLEMENTING DECISION

of XXX

on the equivalence of the legal and supervisory framework applicable to designated contract markets and swap execution facilities in the United States of America in accordance with Regulation (EU) No 600/2014 of the European Parliament and of the Council

(Text with EEA relevance)

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(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 amending Regulation (EU) No 648/2012[1], and in particular Article 28(4) thereof,

Whereas:

(1) Regulation (EU) No 600/2014 requires financial counterparties and non-financial counterparties above the clearing threshold as referred to in Article 4 of Regulation (EU) No 648/2012[2] established in the Union to conclude transactions in derivatives pertaining to a class of derivatives that has been declared subject to the trading obligation only on regulated markets, multilateral trading facilities (MTFs), organised trading facilities (OTFs) and third-country trading venues recognised by the Commission as equivalent. The relevant third country should provide for an effective equivalent system for the recognition of trading venues authorised under Directive 2014/65/EU.

(2) The procedure for recognition of trading venues established in third countries set out in Article 28 of Regulation (EU) No 600/2014 aims to allow financial and certain non-financial counterparties established in the Union to conclude transactions in derivatives subject to the trading obligation on third-country trading venues recognised as equivalent. The recognition procedure and the equivalence decision thus increases transparency of derivatives trading, including where trading takes place in trading venues established in a third country.

(3) Considering the agreement reached by the parties to the G20 in Pittsburgh on 25 September 2009 to move trading in standardised OTC derivative contracts to exchanges or electronic trading platforms, it is appropriate to provide for a suitable range of eligible venues on which trading pursuant to that commitment can take place. The equivalence provisions should be read in the light of the objectives pursued by Regulation (EU) No 600/2014, in particular its contribution to the establishment and functioning of the internal market, market integrity, investor protection and financial stability. Regulation (EU) No 600/2014 underlined moreover the need to establish a

[1] Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (OJ L 173, 12.6.2014, p. 84).

[2] 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 (OJ L 201, 27.7.2012, p. 1)

single set of rules for all institutions in respect of certain requirements and to avoid potential regulatory arbitrage. Therefore, when designating the standardised OTC derivative contracts that will be subject to a trading obligation, it is appropriate that the Union fosters the development of a sufficient number of eligible venues for the execution of the trading obligation, including in the EU.

(4) In accordance with Article 28(4) of Regulation (EU) No 600/2014, third-country trading venues can be recognised as equivalent to trading venues established in the Union where they comply with legally binding requirements which are equivalent to the requirements for the trading venues resulting from Directive 2014/65/EU, Regulation (EU) No 596/2014 and which are subject to effective supervision and enforcement in that third country. This should be read in the light of the objectives pursued by that act, in particular its contribution to the establishment and functioning of the internal market, market integrity, investor protection and ultimately, but no less importantly, financial stability.

(5) Swap trading platforms operating in the United States of America (USA) offer high trading volumes in dollar-denominated swaps and it is important that EU firms are able to access this liquidity for efficient risk management. Taking account of the importance of US swap trading platforms for the functioning of the EU market and their impact on financial stability, it is appropriate, given this context, to recognise swap trading platforms operating in the USA. This decision is based on a detailed assessment of the legal and supervisory framework governing swap trading platforms under the US Commodity Exchange Act (CEA) and implementing regulations with a particular focus on market integrity and transparency.

(6) The purpose of this equivalence assessment is therefore to verify that the legal and supervisory arrangements under the CEA and implementing regulations ensure that designated contract markets (DCMs) and swap execution facilities (SEFs) established in the USA and authorised by the Commodity Futures Trading Commission (CFTC) are subject to legally binding requirements which are equivalent to the requirements for the trading venues resulting from Directive 2014/65/EU of the European Parliament and of the Council[3], Regulation (EU) No 596/2014 of the European Parliament and of the Council[4] and Regulation (EU) No 600/2014 and based on the criteria set out in Articles 28(4) of Regulation (EU) No 600/2014. The purpose of the equivalence assessment is also to verify whether DCMs and SEFs are subject to effective supervision and enforcement in that third country.

(7) Legally binding requirements for DCMs authorised in the USA are set forth in the CEA form of a principles-based legal framework for the operation of DCMs. The CEA's requirements for DCMs include 23 Core Principles. These principles have the force of law and DCMs must comply with them on an initial and ongoing basis. A DCM must also comply with applicable CFTC regulations (CFR), which specify requirements for operating as a DCM.

(8) Legally binding requirements for SEFs authorised in the USA are set forth in the CEA in the form of a principles-based legal framework. SEFs operate under Section 5h of

[3] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

[4] Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC (OJ L 173, 12.6.2014, p. 1).

the CEA, which was added by Section 733 of the Dodd-Frank Wall Street Reform and Consumer Protection Act for the trading and processing of swaps. Section 5h of the CEA sets out 15 Core Principles for SEFs. In order to obtain and maintain registration with the CFTC, SEFs must comply with the 15 Core Principles. A SEF must also comply with CFTC regulations applicable to SEFs on an initial and ongoing basis.

(9) Article 28(4)(a-d) of Regulation (EU) No 600/2014 sets out four conditions that need to be fulfilled in order to determine that the legal and supervisory arrangements of a third country regarding the trading venues authorised therein are equivalent to those laid down in Regulation (EU) No 600/2014 and Directive 2014/65/EU.

(10) According to the first condition set out in Article 28(4)(a) of Regulation (EU) No 600/2014, third-country trading venues must be subject to authorisation and to effective supervision and enforcement on an ongoing basis.

(11) In order to operate as a DCM an applicant must apply for designation with the CFTC and demonstrate compliance with the applicable provisions under the CEA as well as the CFTC regulations. Likewise, in order to operate as a SEF, an applicant must obtain registration with the CFTC and demonstrate compliance with applicable provisions under the CEA as well as the CFTC regulations. The CFTC has regulatory oversight authority over DCMs and SEFs, respectively, pursuant to Sections 5 and 5h of the CEA, 7 USC 7 and 7 USC 7b-3. In order to be designated by the CFTC, a DCM must comply with the 23 DCM Core Principles under the CEA and any requirements that the CFTC may impose by rule or regulation. In order to be registered with the CFTC, a SEF must comply with the 15 SEF Core Principles, under the CEA and any requirements that the CFTC may impose by rule or regulation. A DCM is required to be a trading facility which generally, under the CEA, means a multilateral system in which participants have the ability to execute transactions in accordance with non-discretionary rules. DCMs must provide members with impartial access to their markets and services. The access criteria must be impartial, transparent, and applied in a non-discriminatory manner. In addition, the CEA and CFTC regulations subject DCMs to organisational requirements with regards to corporate governance, conflicts of interest policy, risk management, fair and orderly trading, trading system resilience, clearing and settlement arrangements, admission to trading and compliance monitoring, all of which must be complied with on an ongoing basis. SEFs are swap trading platforms which operate on a multilateral basis. SEFs must provide eligible contract participants with impartial access to their markets and services and are required to have access criteria that are impartial, transparent and applied in a fair and non-discriminatory manner. SEFs are also subject to organisational requirements with regards to corporate governance, conflicts of interest policy, risk management, fair and orderly trading, trading system resilience, clearing and settlement arrangements, admission to trading and compliance monitoring, all of which must be complied with on an ongoing basis.

(12) DCMs and SEFs must establish rules governing their operations, including rules prohibiting abusive trade practices and enforce compliance with these rules. These rules and any amendments thereto are assessed by the CFTC to ensure consistency with the CEA and CFTC regulations. DCMs and SEFs must have the capacity to detect, investigate and apply appropriate sanctions to any person that violates any DCM or SEF rule. DCMs and SEFs are permitted to use regulatory services of a third party for assistance in complying with applicable requirements under the CEA and CFTC regulations. DCMs and SEFs remain responsible for compliance with their

statutory and regulatory obligations, even when using such a third party to provide regulatory services.

(13) The CFTC also has ongoing oversight and enforcement responsibilities with respect to DCMs and SEFs. Regular Rule Enforcement Reviews (RERs) are performed, which are designed to evaluate a DCM's compliance with statutory and regulatory requirements relating to trade practice surveillance, market surveillance, audit trail and DCM disciplinary programs. A similar program is being developed for SEFs. Section 8(a)(1) of the CEA gives the CFTC broad power to conduct investigations to ensure compliance with the CEA and the CFTC regulations. Pursuant to CEA Sections 5e, 6(b), 6b and 6c(a) the CFTC may also bring civil enforcement actions to enjoin violations of the CEA or CFTC regulations and obtain other equitable relief and monetary sanctions: bring administrative enforcement proceedings, suspend or revoke the designation of a DCM or the registration of a SEF, and make and enter against a DCM or SEF a cease and desist order from violating the CEA or CFTC regulations. Section 6(c) of the CEA gives the CFTC power to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence and require the production of books, correspondence, memoranda and other records, for the purposes of enforcing the CEA or for purposes of any investigation or proceeding.

(14) It can therefore be concluded that DCMs and SEFs are subject to authorisation and to effective supervision and enforcement on an ongoing basis.

(15) According to the second condition set out in Article 28(4)(b) of Regulation (EU) No 600/2014, third-country trading venues must have clear and transparent rules regarding admission of financial instruments to trading so that such financial instruments are capable of being traded in a fair, orderly and efficient manner and are freely negotiable.

(16) Neither a DCM nor a SEF may list a new derivative contract unless that contract complies with the CEA and CFTC regulations, which ensure fair, orderly and efficient trading. This is enforced by requiring all DCMs and SEFs to file new contracts with the CFTC prior to listing, either for CFTC approval or with a certification by the DCM or SEF that the contract complies with the CEA and CFTC regulations. The filing must contain an explanation and analysis of the derivative contract, and its compliance with any applicable requirements, including the CEA requirement that a DCM or SEF only list contracts that are not readily susceptible to manipulation. The CFTC guidance for complying with this statutory requirement states that in the case of cash-settled swap contracts, the DCM or the SEF should consider, inter alia, the reliability of the cash settlement price as an indicator of cash market values, as well as the commercial acceptability, public availability, and timeliness of the price series that is used to calculate the cash settlement price. Such guidance also outlines what the CFTC considers to be an acceptable specification of contract terms and conditions. The DCM and the SEF must make the terms and conditions of a derivative contract filed with the CFTC publicly available, at the time of such filing. This pre-listing filing requirement and the CFTC requirements with respect to contract characteristics, help to ensure that derivative contracts are capable of being traded in a fair, orderly and efficient manner. The CFTC guidance assists the CFTC in its consideration of whether a DCM or SEF is in compliance with the requirements of Core Principles.

(17) DCMs are required to provide a competitive, open, and efficient market and a mechanism for executing transactions that protects the price discovery process of trading in the centralized market of the DCM. Consistent with this requirement, all

DCMs utilize central limit order books in which bids and offers are shown. Additionally, DCMs post price quote information on their public websites. SEF transactions involving swaps that are subject to the CFTC's trade execution requirement, which are not block trades, must be executed either in accordance with an Order Book, as defined in the CFTC regulations, or in accordance with a Request-for-Quote System that operates in conjunction with an Order Book. A "Request-for-Quote System" is defined in the CFTC regulations as a trading system or platform in which a market participant transmits a request for a quote to buy or sell a specific instrument to no less than three market participants in the trading system or platform, to which all such market participants may respond. Furthermore, Part 43 of the CFTC's regulations requires a publicly reportable swap transaction to be reported to a CFTC-registered swap data repository (SDR) as soon as technologically practicable after the transaction is executed. For a publicly reportable swap transaction that is executed on or pursuant to the rules of a DCM or SEF, the SDR must ensure that swap transaction and pricing data is publicly disseminated as soon as technologically practicable after such data is received from the DCM or SEF, unless the swap is subject to a time delay. An SDR is required to delay public dissemination of swap transaction and pricing data for publicly reportable swap transactions that exceed certain sizes.

(18) It can therefore be concluded that DCMs and SEFs have clear and transparent rules regarding admission of financial instruments to trading so that such financial instruments are capable of being traded in a fair, orderly and efficient manner and are freely negotiable.

(19) According to the third condition set out in Article 28(4)(c) of Regulation (EU) No 600/2014, issuers of financial instruments must be subject to periodic and ongoing information requirements ensuring a high level of investor protection.

(20) Given the nature and characteristics of the derivative contracts listed on DCMs and SEFs, and in particular the fact that their underlying assets are primarily commodities, interest rates or currencies, the third condition cannot be applied to most of the options and swaps transacted on DCMs and SEFs. This requirement cannot apply to derivative contracts which do not reference equities as an underlying. For the derivatives subject to the trading obligation, such as swaps, with interest rates as an underlying, there is no company that could issue relevant financial reports. Disclosure obligations are however incumbent on issuers of derivative contracts where an underlying asset is a security. In the USA, this would only concern options on securities or security-based swaps. Options on securities can only be traded on a securities exchange under the jurisdiction of the Securities and Exchange Commission (SEC), therefore not on either DCMs or SEFs. Security-based swaps may be transacted on a security-based swap execution facility, but they are regulated by the SEC. Where the underlying security of a security-based swap is admitted to trading on a US national securities exchange, its issuer is subject to the reporting requirements under Section 13(a) of the Exchange Act and must publish annual and interim financial reports, for which the US regulatory framework has clear, comprehensive and specific disclosure requirements, and the free public access of which is ensured by the EDGAR system provided by the SEC's website. Thus, as a result, a high level of investor protection is still ensured.

(21) According to the fourth condition set out in Article 28(4)(d) of Regulation (EU) No 600/2014, the third-country framework must ensure market transparency and integrity via rules addressing market abuse in the form of insider dealing and market manipulation.

(22) The CEA and CFTC regulations establish a comprehensive regulatory framework to ensure market integrity and prevent insider dealing and market manipulation. This framework prohibits, and authorises the CFTC to take enforcement action against conduct which could result in distorting the functioning of the markets such as price manipulations and communication of false or misleading information (CEA §§ 6(c) and 9(a)(2), §§ 180.1 and 180.2 of the Commission's regulations), trade practice violations (CEA §§ 4c(a)(1)-(2)), certain disruptive practices that could impair the orderly execution of transactions (CEA § 4c(a)(5)) and the use, or attempted use, of a manipulative device, scheme or artifice to defraud (CEA § 6(c)(1), 17 CFR § 180.1 of the Commission's regulations) Trading on the basis of unlawfully obtained inside information or in breach of a pre-existing duty to disclose material non-public information may also be a violation of the CEA. DCMs and SEFs have the responsibility to monitor their markets to help ensure that trading activities are subject to ongoing and effective surveillance and in order to detect and prevent manipulative activity that could result in price distortion or market manipulation. The CFTC's RER program evaluates a DCM's surveillance and disciplinary programs. A similar program is being developed for SEFs. Furthermore, the CFTC can, at any time and on its own initiative, request a DCM or a SEF to demonstrate that it is in compliance with obligations of the DCM or SEF under the CEA or the CFTC regulations.

(23) It can therefore be concluded that the framework applicable to DCMs and SEFs in the US ensures market transparency and integrity via rules addressing market abuse in the form of insider dealing and market manipulation.

(24) It can therefore be concluded that DCMs and SEFs comply with legally binding requirements which are equivalent to the requirements for the trading venues resulting from Directive 2014/65/EU, Regulation (EU) No 596/2014 and Regulation (EU) No 600/2014 and are subject to effective supervision and enforcement in that third country.

(25) In accordance with Article 28(1)(d) of Regulation (EU) No 600/2014 third-country trading venues can be recognised as equivalent provided that the third country provides for an effective equivalent system for the recognition of trading venues authorised under Directive 2014/65/EU to admit to trading or trade derivatives declared subject to the trading obligation in that third country on a non-exclusive basis.

(26) Pursuant to CEA, Section 5h(g), the CFTC is authorized to exempt swap execution facilities from registration if the CFTC finds that the facilities are subject to comparable, comprehensive supervision and regulation on a consolidated basis by the national competent authorities in the home country of the facility. In accordance with Section 5h(g), the CFTC is empowered to exempt all regulated markets, MTFs and OTFs notified by the Commission through a single order once the CFTC determines that the notified venues are subject to comparable and comprehensive supervision and regulation on a consolidated basis.

(27) A joint statement by the Chairman of the CFTC and the Vice President of the European Commission responsible for financial services sets out the CFTC's approach concerning exemption of EU trading venues. The decision will also be complemented by cooperation arrangements to ensure the effective exchange of information and coordination of supervisory activities between the national competent authorities responsible for the authorisation and supervision of the recognised EU trading venues and the CFTC.

(28) It can therefore be concluded that the legal and supervisory framework of the USA provides for an effective equivalent system for the recognition of trading venues authorised under Directive 2014/65/EU to admit to trading or trade derivatives declared subject to trade execution requirement in the USA on a non-exclusive basis.

(29) This decision determines the eligibility of third-country trading venues to allow financial and non-financial counterparties established in the Union to comply with their trading obligation when trading derivatives on a third-country venue. This decision does therefore not affect the ability of financial and non-financial counterparties established in the Union to trade derivatives that are not subject to the trading obligation in accordance with Article 32 of Regulation (EU) No 600/214 on third-country trading venues.

(30) This Decision is based on the legally binding requirements relating to DCMs and SEFs applicable in the USA at the time of the adoption of this Decision. The Commission should continue monitoring on a regular basis the evolution of the legal and supervisory arrangements for these trading venues, market developments, the effectiveness of supervisory cooperation in relation to monitoring and enforcement and the fulfilment of the conditions on the basis of which this Decision has been taken.

(31) The regular review of the legal and supervisory arrangements applicable in the USA to DCMs and SEFs authorised therein and market developments is without prejudice to the possibility of the Commission undertaking a specific review at any time where relevant developments make it necessary for the Commission to re-assess the equivalence granted by this Decision. Such re-assessment could lead to the repeal of this Decision.

(32) The measures provided for in this Decision are in accordance with the opinion of the European Securities Committee,

HAS ADOPTED THIS DECISION:

Article 1

For the purposes of Article 28(4) of Regulation (EU) 600/2014 the legal and supervisory framework of the Unites States of America applicable to designated contract markets and swap execution facilities authorised therein and set out in the Annex shall be considered to be equivalent to the requirements laid down in Regulation (EU) No 600/2014 for trading venues as defined in Directive 2014/65/EU.

Article 2

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

Done at Brussels,

For the Commission
The President
Jean-Claude Juncker