Linklaters

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Sip n Learn: Intro to the Newest Clearing Model: EATM

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1 What is the EATM?

The European Agent Trustee Model ("**EATM**") is a new client clearing model for Europe. The EATM has been designed broadly to replicate the US FCM Model in Europe and will be complementary to, and not a substitute for, other clearing models available for use in Europe.

The key driver behind the EATM is to increase capacity in the client clearing market. It is hoped that capacity will be increased by the cost savings and efficiencies that will be realised by clearing members ("**CMs**") providing client clearing services under the EATM, rather than pursuant to the existing clearing model in Europe (the "**Principal Model**"). The capacity of CMs has become of particular importance in recent years as the number of CMs in the market reduces. It is hoped that the EATM will provide a welcome solution to this issue.

The EATM is currently available for use by CMs incorporated in England and Wales and their Clients (who may be incorporated in any jurisdiction) at LCH Limited. A second version of the EATM for German CMs is also in development. In due course, it is intended that both the English and German law versions of the EATM will be offered at both LCH Limited and Eurex Clearing.

The EATM has been designed (to the extent possible) to be jurisdiction-neutral in nature, such that the core structure can be recreated for use by CMs incorporated in other jurisdictions if the English or German law structures would be effective on the insolvency of CMs incorporated in those jurisdictions. The EATM has also been designed with a view to its replication under other legal systems if the English or German law structures would not be suitable.

The EATM has been designed for initial implementation in respect of OTC contracts, but with a view to its extension to exchange/venue traded contracts. It is product agnostic.

2 Structure of the EATM

Under the EATM, transactions ("**Client Transactions**") entered into by a CM with a central counterparty (a "**CCP**") are held by the CM for the account of one or more Clients. Payments and collateral will fall outside this arrangement. The precise nature of this arrangement differs as between different versions of the EATM. Under the English law version of the EATM (the "**English Model**"), the CM will hold Client Transactions as a trustee. Under the German law version of the EATM (the "**German Model**"), the CM will hold Client Transactions as a trustee (*Treuhänder*) in connection with a commercial mandate (*Geschäftsbesorgungsverhältnis*).

3 English law trustee arrangement

The general feature of an English trustee arrangement is that a person in whom property is vested (the 'trustee') is compelled in equity to hold the property for the benefit of another person (the 'beneficiary').[1]

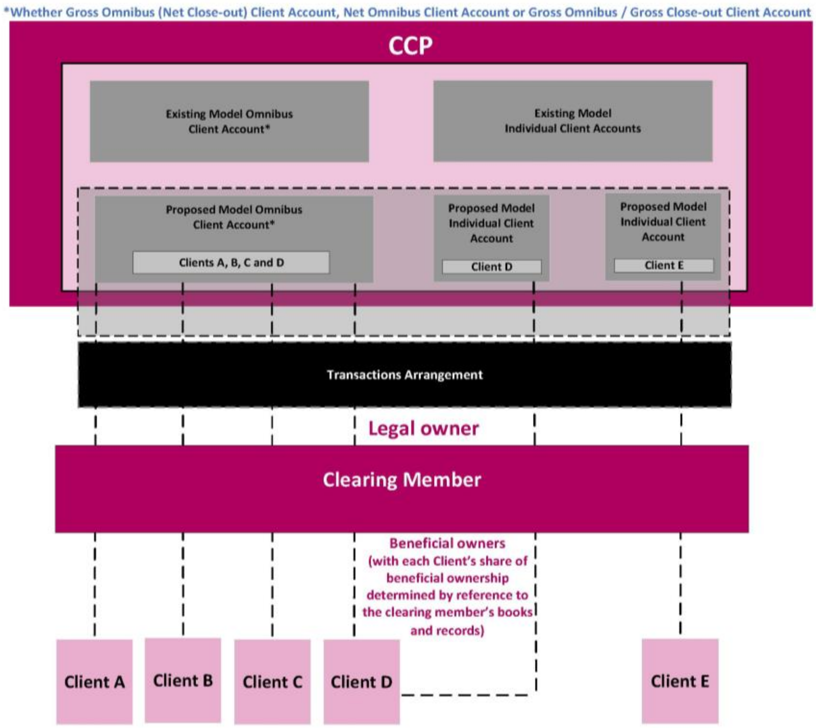
Under the EATM, the "trust property" comprises the claims that a CM has against the CCP in respect of Client Transactions. In more precise terms, the trust property will be each claim that a CM has against a CCP in respect of each such Client Transaction, including any right of the CM to any payment or delivery under such Client Transactions and any right of the CM to the transfer or re-transfer of margin either in respect of an individual Client Transaction or multiple Client Transactions. Under the English Model, there is a single trustee

[1] John McGhee, QC, Steven Elliott, QC, and others (eds), *Snell's Equity* (34th Edn, Sweet & Maxwell 2020) para 21-001.

arrangement over all Client Transactions entered into with all CCPs by a single CM on behalf of each of its Clients (i.e. there is one trust per CM, rather than one trust per Client, account or CCP).

Any cash, securities and other assets transferred to the CM by a CCP as payments under Client Transactions or transfers of collateral will not be trust property (other than for the very brief period when first received by the CM from the CCP). On receipt of such cash, securities or other assets, the CM will assume a contractual delivery obligation to the relevant Client for equivalent assets under the client clearing agreement with such Client, and such cash, securities or other assets will immediately cease to be trust property.

Figure 1: English Model trust over all Client Transactions of a CM at the CCP



4 How is the EATM different from the US FCM Model and existing client clearing models in Europe?

The EATM has been designed to replicate the US FCM Model and so there are not a significant number of differences between the two.

The main difference is the fact that, under the EATM, collateral flows are kept outside the applicable client assets regime in the jurisdiction of the CM (unlike under the US FCM Model).

Unlike under the US FCM Model, under the EATM, the Client will not grant security in favour of the CM over its rights under the client clearing agreement (including its rights under the trustee arrangement). This is because such a security interest would, as a practical matter, not materially mitigate the CM's credit risk exposure to the Client.

It is also worth noting that, under the US FCM Model, the FCM is an "agent-trustee" which is a form of agency relationship under applicable US law, whereby the FCM holds the Client Transactions for the account of its Client as a trustee that also acts as an agent for the Client. Under the EATM, the CM holds the Client Transactions for the account of its Client(s) as a trustee.

The main difference between the EATM and the existing client clearing model in Europe (the "**Principal Model**") is that the back-to-back transactions between the CM and the Client under the Principal Model are replaced under the EATM by the trustee arrangement. Under the EATM, the CM will be party to one transaction – the Client Transaction with the CCP, whereas under the Principal Model, it is party to two transactions – one with the CCP and one with the Client.

5 How is the EATM documented? Do Clients need to enter into a new Client Clearing Agreement with their CMs?

Due to its unique nature, it is not possible to document the EATM under existing template client clearing documentation available in Europe (without substantive amendments being made to such documentation).

The FIA has therefore published a new form of client clearing agreement for the EATM, the FIA Client Clearing Agreement 2025 – EATM (English Law Agreement and Terms) (the "**CCA**"). The CCA is based on the FIA 2018 Terms of Business, as supplemented by "Segregated Asset Terms" which set out the terms of the trustee arrangement pursuant to which the CM will hold Client Transactions on behalf of its Client.

The existing terms of the FIA 2018 Terms of Business have been retained to the extent possible in the CCA, but amendments have had to be made to accommodate the EATM (e.g. as there is no back-to-back transaction governed by the client clearing agreement, it has been necessary to create additional payment obligations under the client clearing agreement pursuant to which the Client will fund amounts due under the Transaction between CM and CCP and the CM will pass on amounts received from the CCP to the Client).

The CCA contains the following broad categories of provisions:

(i) clauses establishing the general relationship between the Client and the CM and the scope of the services to be provided by the CM to the Client pursuant to the CCA;

(ii) clauses concerning the provision of margin (which includes both collateral and payments under Transactions) to cover exposures arising in connection with the services provided by the CM to the Client under the CCA and establishing the mechanism through which the CM will account to the Client for payments and other deliveries due to the Client in respect of Client Transactions;

(iii) clauses providing for the conversion of Client Transactions from being held under the EATM to the Principal Model and vice versa, the porting of transactions and the entry into of offsetting transactions;

(iv) clauses containing representations, covenants and events of default and other triggers for the termination of Client Transactions and/or the CCA (excluding voluntary termination), as well as the effect of the termination and transfer of Client Transactions and the CCA and the Client's and CM's rights in such circumstances;

(v) clauses concerning limited recourse, set-off, liability, voluntary termination and other boilerplate provisions;

(vi) an Annex to allow the specification of elections under the CCA; and

(vii) a Schedule containing the "Segregated Asset Terms", being the terms governing the trustee arrangement pursuant to which the CM holds rights against certain CCPs that arise in relation to Client Transactions on trust for, *inter alia*, the Client.

As noted above, the Segregated Asset Terms are appended to the CCA executed by a CM and each of its Clients. However, individual Segregated Asset Terms cannot be negotiated for each Client (due to there being a single trust per CM). Once the Segregated Assets Arrangement has been constituted, attaching the Segregated Asset Terms to any subsequently executed EATM Agreement will have no legal effect, but rather, in practical terms, will make clear the terms of the Segregated Assets Arrangement to each Client.

6 Can Clients use both the EATM (English Model) and the Principal Model?

(i) A Client <u>will not</u> be able to clear under both the EATM and Principal Model with the same CM at the same CCP in respect of the same CCP service.

(ii) A Client <u>can</u> clear under both the EATM and Principal Model at different CCPs via the same CM.

(iii) A Client <u>can also</u> clear under both the EATM and Principal Model at the same CCP via the same CM, provided that this is respect of different CCP services offered by that CCP.

(iv) Clients may access the same CCP service (and, therefore, the same CCP) using different CMs who may provide their clearing services through different models (the EATM or Principal Model). A Client could, therefore, be offered the EATM through one CM and the Principal Model through another CM at the same CCP (and even in respect of the same CCP service). However, in certain cases a CCP may restrict a Client from clearing at that CCP via different CMs using different models. If such restriction applies, and the Client is accordingly only permitted to clear certain transactions at a certain CCP service through one CM, the Client will need to elect whether it uses the EATM or Principal Model for that CCP service (in respect of which the CM provides clearing services).

Provisions have also been included in the CCA to allow Clients to migrate from the Principal Model to the EATM and vice versa (both in a non-default and via porting in a default scenario).

7 How is client margin/collateral treated under the EATM?

Collateral will be transferred between the CM and CCP in accordance with the CCP's rulebook, which could be by way of security or title transfer.

Collateral will be transferred between the CM and Client by way of title transfer. There is currently no ability for Clients to transfer collateral to their CMs under the EATM by way of security or for CMs to offer a client asset solution in respect of transfers of collateral. Transfers of collateral between the CM and Client should operate (from an operational perspective) in the same manner as any transfers by way of title transfer would under the Principal Model, although there are some legal differences in the way transfers of collateral are treated under the EATM.

As noted above, although the CM's right to the transfer of collateral will be held for the Client subject to the trustee arrangement, the collateral actually transferred by the CCP to the CM will not be held subject to the trustee arrangement (other than, in the case of the English Model, for the very brief period when first received by the CM from the CCP).

8 What happens on: (i) a client default (including porting and leapfrog payments), (ii) a CM default and (iii) a CCP default under the EATM?

(i) Client Default

Under the EATM, the CM has the right to deal with Client Transactions as principal on the default of the Client. It can therefore take any of the steps it typically would under the Principal Model should its Client default (e.g. moving the Client Transactions to its house account and entering into offsetting transactions with the CCP).

The CM will account to the Client for any amounts it receives from the CCP in respect of the Client Transactions or gains that it makes from liquidating or closing out the Client Transactions of a defaulting Client and will require payment from the Client (or otherwise deduct such amount from the Client's collateral balance) for any costs or losses incurred by the CM in respect of such Client Transactions, including any amounts owed to the CCP by the CM.

(ii) CM Default

As under the Principal Model, on the default of the CM, the CCP will try to port the Client Transactions and associated collateral held by the CCP to another CM of the Client. Client Transactions and associated collateral can either be ported to a CM and maintained under the EATM or be ported and become subject to the Principal Model.

If porting is not possible, the Client Transactions will be closed out. In accordance with its obligations under EMIR[2] or UK EMIR[3], the CCP will be required to transfer any amounts owed by the CCP in respect of the terminated Client Transactions directly to the Client. If this is not possible, the CCP will be required to transfer any such amounts to the CM for the account of the Client.

If any amounts are owed from the Client to the CM, the Client will be required to pay the CM (or such amounts will be deducted from the collateral balance held by the CM and owed by the CM to the Client) in accordance with the terms of the CCA.

(iii) CCP Default

Upon the default of the CCP, any amount owed by the CCP to the CM will be held by the CM subject to the trustee arrangement on behalf of the Client. Once payment is made by the CCP to the CM, the CM will be under a contractual duty to account for such amount to the Client pursuant to the terms of the CCA.

If any amounts are owed from the CM to the CCP, the CM may claim such amounts from the Client under the CCA (or such amounts will be deducted from the collateral balance held by the CM and owed by the CM to the Client).

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[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

[3] Regulation (EU) No 648/2012 as it forms part of domestic law

9 How does close-out netting operate under the EATM?

Close-out netting between the CCP and CM in respect of the Client Transactions will operate in accordance with the provisions of the CCP rulebook. The trustee arrangement is over the rights of the CM against the CCP under the CCP's rulebook in respect of the Client Transactions (and associated collateral) and designed in a way that maintains mutuality between the CM and the CCP for purposes of close-out netting and set-off. Therefore, the trustee arrangement should not impact the operation of netting or set off under the CCP rulebook.

There will be no close-out netting in respect of amounts owing under the CCA between the CM and Client because the CCA does not give rise to separate underlying transactions between the CCP and the CM. Instead, the CM will maintain a running balance of what it owes to the Client, or what the Client owes to it (referred to in the CCA as the "Title Transfer Balance"). This will cover all payments, margin and other amounts owing between the CM and Client. The liability of the CM and the Client to each other in respect of the Title Transfer Balance reflects the net liability between the CM and the Client.

10 Will the EATM require significant changes to the operational processes of CMs and CCPs?

Although the EATM was designed with a view to minimising the impact on CMs' and CCPs' current processes, some changes are inevitably required.

As Client Transactions subject to the EATM cannot be commingled in an account with Client Transactions under the Principal Model, CCPs will need to set up separate client accounts for Client Transactions subject to the EATM. These accounts should be able to mirror the CCP's current account offering for the Principal Model (as the EATM does not require a different level of segregation or account set-up than the Principal Model).

Similarly, depending on CMs' existing approach to maintenance of books and records, some amendments may need to be made to CMs' records to clearly record that each Client Transaction is held on behalf of their Clients pursuant to a trustee arrangement.

11 Are there legal opinions supporting the EATM?

The FIA are commissioning new legal opinions which will cover the enforceability of the CCA, including the trustee arrangement, close-out provisions and margin provisions.

Opinions will be commissioned covering enforceability of the EATM pre and post insolvency of the Client, CM and CCP for each jurisdiction in which Clients and CMs may be located.

Linklaters published the English legal opinion on the EATM in September 2025. The English legal opinion broadly covers:

(i) recognition of English law as the governing law of the CCA;

(ii) enforceability of the CCA and Segregated Assets Arrangement (including valid creation of an English law trust via fulfilment of the "Three Certainties"[4]) pre and post insolvency of the CM and Client (to the extent the Client is an English entity);

[4] *Knight v Knight* (1840) 3 Beav. 148 provides that, in order for there to be a valid trust under English law, there must be: (i) certainty of intention to create a binding legal obligation to hold property for another; (ii) certainty of the property which is the subject of the trust; and (iii) certainty of the beneficiaries of that trust.

(iii) the Segregated Assets Arrangement will preserve the effect of set-off and netting arrangements that may apply pursuant to the rules of the relevant CCP;

(iv) the CCA gives rise to a single contingent contractual claim of either the CM or the Client in relation to the Title Transfer Balance (or any shortfall in respect thereof) under the CCA, which does not arise by operation of contractual set-off or netting, but instead pursuant to a running account mechanism and such claim will be legal, valid and enforceable prior to, and following, the insolvency of the CM and Client (to the extent the Client is an English entity);

(v) the margin provisions under the CCA will constitute a "title transfer collateral arrangement" for the purposes of The Financial Collateral Arrangements (No.2) Regulations 2003;

(vi) enforceability of porting of Client Transactions and efficacy of leapfrog payments from the CCP following the default of the CM; and

(vii) that the CCA will not give rise to a "collective investment scheme"[5] under the Financial Services and Markets Act 2000.

[5] A collective investment scheme (CIS) is an arrangement that enables investors to contribute to, and effectively 'pool' their respective assets within, a fund scheme and have these professionally managed by an independent manager. The manner in which CIS are set up and operated in England and Wales is regulated and so it is necessary to conclude that the EATM would not be subject to those regulations.