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From:	Presidency
To:	Working Party on Financial Services and the Banking Union (EMIR/CCP) Financial Services Attachés

Subject:	Presidency non-paper on certain measures for a safe and resilient EU clearing system
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Ministry of Finance
Financial Markets and Institutions Department



Presidency non-paper on certain measures for a safe and resilient EU clearing system

Introduction

The COM's proposal contains a set of targeted amendments to the EMIR framework with a view to make the Union's clearing system and EU CCPs safer and more resilient, thus better able to withstand economic shocks. Several of the changes are proposed against the background of the developments in energy derivatives markets in 2022 and the risks and issues that were displayed.

The proposed measures were presented at the Council Working Party on 3 February where MS were invited to provide initial remarks on the relevant Articles (4a, 9, 10, 11, 14(3), 26, 37, 38, 41, 44, 46) in EMIR. Subsequently, MS had the occasion to follow up with written comments on the changes proposed. The PCY has taken note of the comments provided both orally and in writing. This PCY paper sets out areas and questions for further in-depth discussions on a few key issues identified (Articles 9, 37, 46).

Areas for examination

During the Council Working Party and further elaborated in the written comments, several MS welcomed the aim of the proposal. However, some of the proposed changes have raised questions and indicated different views among MS.

The PCY invites MS to give guidance on the following issues:

1. Eligible collateral
2. Requirements for NFC participation in a CCP
3. Removal of the exemption for reporting of intragroup transactions

1. Eligible collateral

Under Article 46(1) of EMIR, a CCP may accept bank guarantees as collateral for non-financial counterparties. The conditions for a commercial bank guarantee to be accepted as collateral under Article 46(1) of EMIR are specified in COM Delegated Regulation 153/2013, Section 2 of Annex I. Among these conditions are that the bank guarantee is issued to guarantee a non-financial clearing member and that it is fully backed by collateral that meets certain conditions. Point 2 of Section 2 of Annex I also adds some specific provisions for guarantees issued by central banks to be accepted as collateral.

Against the price and volatility increases in energy markets, causing increases in CCPs' margin requirements and resulting in liquidity strains for non-financial counterparties, ESMA was requested by the COM in September 2022 to review whether the collateral requirements could be temporarily adjusted. ESMA responded to the request and subsequently the COM Delegated Regulation 153/2013 was amended to temporarily extend the eligible collateral. From 29 November 2022 to 29 November 2023, the requirement that a bank guarantee be fully backed does not apply for certain energy-related derivatives. That is, during this 12-month period, uncollateralised bank guarantees are eligible as collateral for non-financial counterparties that are acting as clearing members. In addition, during the same period public guarantees that meet the conditions set out in Section 2a of Annex I shall be considered as highly liquid collateral and hence be eligible as collateral for all counterparties.

In the current proposal, the COM proposes to extend the eligible collateral to also include bank guarantees (both public bank and commercial bank guarantees) as well as public guarantees, by way of introduction in the Level 1 text of EMIR. This would be specified in Article 46(1) of EMIR. In particular, the eligibility of bank guarantees as collateral would be extended to financial counterparties in addition to non-financial counterparties. The bank guarantees and public guarantees may be accepted by the CCP provided that they are unconditionally available upon request within the liquidation period.

MS initial remarks, both in the first Working Party and in written comments, indicate that the extension of eligible collateral is an issue that warrants further consideration and discussion. Among the MS expressing their views

at this stage, views are mixed. On the one hand, the proposed extension of eligible collateral is welcomed by some MS. On the other hand, other MS are hesitant, given the interconnectedness of the financial system. Several MS ask for clarifications on the objective of the amendments and its implications for the scope of eligible collateral, e.g. in relation to the provisions of the current Level 1 text and the temporary regulatory technical standard. Further assessment of the measure is called for. In addition, several MS stress the potential risks from a permanent extension of eligible collateral in line with the proposal, notably contagion risks to other market participants, such as CCPs and public entities, and other sectors of the economy. In particular, the credit risk of commercial bank guarantees has been mentioned.

MS are invited to provide their views on the following questions and possible ways forward:

Q1: Do you agree with the COM's proposal to include bank guarantees as eligible collateral for all counterparties? If not, why?

Q2: Should bank guarantees be eligible as collateral only for certain counterparties? If so, which ones and why?

Q3: Should there be specific additional safeguards in place in EMIR as regards the eligibility of bank guarantees? If yes, which ones?

Q4: Should public guarantees and public bank guarantees be eligible for all types of counterparties? Should there be specific additional safeguards in place in EMIR? If yes, which ones?

2. Requirements for NFC participation in a CCP

Article 37 of EMIR lays down the requirements for participation in a CCP. Paragraph 1 of that Article states that: *A CCP shall establish, where relevant per type of product cleared, the categories of admissible clearing members and the admission criteria, upon the advice of the risk committee pursuant to Article 28(3). Such criteria shall be non-discriminatory, transparent and objective so as to ensure fair and open access to the CCP and shall ensure that clearing members have sufficient financial resources and operational capacity to meet the obligations arising from participation in a CCP. Criteria that restrict access shall be permitted only to the extent that their objective is to control the risk for the CCP.*

In addition to the current requirement that clearing members shall have *sufficient financial resources and operational capacity*, the COM proposes to further

specify the conditions to be met for non-financial counterparties to be accepted as clearing members. In Article 37, the inclusion of paragraph 1a is proposed, the first paragraph of which states that: *A CCP shall accept non-financial counterparties as clearing members only if they are able to demonstrate that they are able to fulfil the margin requirements and default fund contributions, including in stressed market conditions.*

ESMA is also mandated to develop draft regulatory technical standards further specifying what is to be considered in a CCP's admission criteria.

Moreover, the proposed paragraph 1a limits the activity of non-financial clearing members: *A non-financial counterparty acting as a clearing member shall not be permitted to offer client clearing services and shall only keep accounts at the CCP for assets and positions held for its own account.*

In addition, the competent authority of a CCP accepting non-financial counterparties as clearing members shall regularly review the arrangements of accepting non-financial counterparties as clearing members. It shall report to ESMA and the college on their appropriateness and ESMA may, following an ad-hoc peer review, issue an opinion or a recommendation on the appropriateness.

MS initial remarks, both in the first Working Party and in the written comments, are mixed. Several MS welcome the proposal. Other MS oppose, or are hesitant towards, the new participation requirements for NFCs, raising questions about the rationale for the measures, the applicability and consequences of such additional requirements. Concerns are also raised about the access to central clearing for non-financial counterparties, including energy companies.

On the one hand, MS stress that in general requirements for non-financial counterparties are lower than for financial counterparties, which calls for additional requirements. On the other hand, some MS refer to the current requirement for clearing members to have *sufficient financial resources and operational capacity* and whether this does not already cater for the ability to fulfil margin requirements and default fund contributions. Moreover, it is highlighted that it may not be easy for a counterparty to demonstrate its ability to fulfil the margin requirements and default fund contributions. It is also noted that participation criteria shall be non-discriminatory.

The proposal on the competent authority's review of the arrangements of accepting non-financial counterparties as clearing members is opposed by some MS. Comments are also provided to the other amendments to Article 37, among others regarding the possibilities for a non-financial counterparty acting as a clearing member in relation to entities within the same group.

MS are invited to provide their views on the following questions and possible ways forward:

Q5: Do MS consider that the existing participation requirements are enough to cover the ability of all counterparty types to fulfil margin requirements and default fund contributions?

Q6: How can access to central clearing by non-financial counterparties be ensured while reducing the potential risk for liquidity issues related to volatile margin requirements?

Q7: Do MS agree on the need for an ESMA mandate to further specify the elements to be considered in the admission criteria of CCPs?

Q8: Do MS agree that NCAs should regularly review the arrangements of accepting non-financial counterparties as clearing members and report to ESMA and the college on their appropriateness?

3. Removal of the exemption for reporting of intragroup transactions

Article 9 of EMIR lays down the reporting obligation under EMIR. The provision implies that counterparties and CCPs shall ensure that the details of any derivative contract they have concluded and of any modification or termination of the contract are reported to a trade repository.

EMIR REFIT introduced the possibility for exemption from the reporting obligation for derivatives contracts within the same group where at least one of the counterparties is a non-financial counterparty or would be qualified as a non-financial counterparty if it were established in the Union, provided that certain conditions are met. A counterparty that intends to apply the exemption shall notify its competent authority and fulfil the conditions for exemption.

The rationale for introducing this exemption was that intragroup transactions involving non-financial counterparties do not significantly contribute to systemic risk and interconnectedness. At the same time, the

obligation to report such transactions imposes significant costs and burdens on non-financial counterparties.

The COM proposes to delete the possibility for exemption from the reporting obligation for intragroup transactions, as proposed by ESMA in their letter to the COM on 22 September 2022. The aim is to provide more visibility on intragroup transactions and the COM notes the potential interconnectedness with the rest of the financial system and recent market developments.

MS initial remarks, both in the first Working Party and in the written comments, display mixed views on the proposal.

Some MS support the removal of the exemption from intragroup transaction reporting, while some MS oppose the removal and see merit in preserving it. Need for clarification is raised regarding intended application. On the one hand, several MS question the benefit of removing the exemption and raise potential significant effects and additional costs for non-financial counterparties and the hedging activities of their groups, particularly given the exemption's recent introduction. On the other hand, the need is also raised to have a clearer picture of the risk exposures of non-financial counterparties and to ensure that relevant authorities are able to effectively monitor risks. A cost-benefit analysis is suggested to ensure proportionality.

MS are invited to provide their views on the following questions and possible ways forward:

Q9: Would MS be in favour of keeping the exemption for:

a) All counterparties

b) A subset of counterparties? If yes, which ones and why?

Q10: If (b) how could that subset be defined? E.g., type of counterparty, activity or sector, or certain classes of derivatives?