Strengthening EU clearing: key issues and way forward proposed

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1. Central clearing has grown in significance since the 2008 financial crisis

Central counterparties (CCPs) have become key components of efficient and stable capital markets. They play a major role in the stability and safety of highly interconnected capital market ecosystems, allowing a centralised netting of risk exposures and a reduction of counterparty risk[1] and also improving the visibility on position concentrations and counterparty credit risk exposures. CCPs also help the financial ecosystem to withstand potential market stresses and economic shocks by mitigating contagion risks and facilitating a more effective hedging of risks. CCPs moreover provide significant efficiency benefits, thanks to the netting of risk exposures and the possibility of using collateral for the clearing of different operations, which are amplified by scale and network effects[2]. CCPs also allow counterparties to maintain a single net exposure to the CCP instead of a complex network of bilateral exposures to individual counterparties.

The role of central clearing has grown significantly with the implementation of the G20 2009 commitments set out following the 2008 financial crisis, which mandated the central clearing of all standardised OTC derivative contracts in order to increase transparency in the OTC derivative market and mitigate the systemic risks generated by these transactions. Between 2008 and 2020, the share of derivative contracts that were centrally cleared rose from 50% to 83% and reached 91% for certain asset classes such as interest rate derivatives (IRD)[3].

In parallel derivative markets have also grown significantly over the last two decades. The global aggregate size of the over-the-counter (OTC) and exchange-traded derivatives (ETD) markets grew from € 78 trillion to € 528 trillion between 1998 and 2020, in terms of notional amounts outstanding. The OTC segment accounts for 90% of that, of which interest rate derivatives (IRD) make up the vast majority (80%).

The mandatory clearing of standardized OTC derivative contracts was implemented in the EU through the EMIR regulation adopted in 2012, which also regulates more broadly the operations of CCPs. The financial stability risks from the possible failure of a CCP, in a context of a growing importance of these infrastructures in the financial system, were also tackled with the CCP recovery and resolution regulation and an enhancement of supervision.

2. Key challenges and areas of improvement concerning central clearing in the EU

CCPs based in the EU and the UK have demonstrated their continued resilience over the last few years, notably during the stress events of 2020 and 2022. However the issues created by Brexit and margin procyclicality remain to be fully tacked and new challenges are emerging in the clearing space.

2.1 Reliance of the EU on UK-based central clearing for euro-denominated derivatives

The reliance of the EU27 on UK-based CCPs handling a significant part of euro-denominated derivatives[4], became a subject of heated debate between the EU and UK, following the decision of the UK to leave the EU. UK-based CCPs indeed play a key role in the clearing of euro-denominated derivative contracts (and also derivatives denominated in other currencies such as the dollar). In the first half of 2021 for example, 91% of all euro-denominated interest-rate swaps (IRS) trades were cleared in the UK[5]. Following Brexit, a temporary recognition was granted to UK-based CCPs (LCH, ICE and LME) due to their importance for the EU financial system. It was extended in 2022 until the end of June 2025.

1. The use of derivatives involves the posting of margin – typically in the form of cash collateral – as a performance guarantee. CCPs guarantee the performance of transactions and contracts by interposing themselves between the parties to a trade through the legal operation of novation, collecting guarantees and becoming the buyer to every seller and the seller to every buyer.
2. Due to network effects, the more users join a CCP, the more value each of them derives from its service in theory. A larger number of users increases netting benefits, increases risk diversification potential and the possibility of using portfolios of collateral for the clearing of various obligations and also reduces transactional and operational costs due to economies of scale.
3. See CEPS 2021, "Setting EU CCP policy – much more than meets the eyes.
4. More than 30% of all OTC derivatives are denominated in euro and other Union currencies.
5. See Capital Markets Law Journal 2023, "CCP supervision after Brexit: from extraterritoriality to a model of shared control". IRS are the largest component of the IRD market. UK-based CCPs also clear about 97% of notional US dollar IRD.

The EU authorities emphasize the potential financial stability risks for the EU posed by the large amounts of euro-denominated contracts cleared in the UK and the possible implications this may have in terms of conduct and transmission of the EU's monetary policy. Although this issue may be addressed to a certain extent by aligned standards and close supervisory cooperation in normal market conditions[6], the EU authorities are concerned by the difficulty for EU regulators and supervisors of handling appropriately financial stability risks for the EU in a crisis situation, with such exposures and with detailed requirements potentially diverging over time. As noted by ESMA[7], in times of crisis, changes to the eligible collateral, margins or haircuts decided by the CCP or the UK authorities may negatively impact the sovereign bond markets of one or more Member States, and more broadly EU financial stability, if they do not fully take into account EU needs. Disruptions in key markets relevant for EU central banks' monetary policies may also hamper the transmission mechanism of those policies. The objective of building a robust and competitive clearing capacity in the EU that remains open to global financial markets via equivalence decisions[8] has therefore been highlighted as an important objective of the EU open strategic autonomy agenda.

For their part, the UK authorities have been stressing the fact that derivative markets are cross-border by nature and the financial stability benefits of cross-border clearing. In their view, resilient cross-border CCPs, such as those established in the UK, support a wider netting of positions across counterparties, currencies and products, leading to a significant diversification of risks and also greater efficiency through economies of scope and scale, which may increase incentives to hedge risks. The UK also considers that after having on-shored the EU clearing legislation and having aligned resolution rules with FSB guidance, UK-based CCPs follow equivalent standards to EU-based ones that can be enforced through close cooperation between the EU and UK authorities. Changes have also recently been made to the statutory objectives of the Bank of England in terms of regulation to ensure that the impacts of the UK's decisions on financial stability in other jurisdictions are adequately taken into account.

2.2 Margin procyclicality issues

The procyclical effects of margin requirements and the possible spill-over of risks to the wider financial system are a second issue that is currently being reviewed by the EU authorities and global standard setters.

An increase of margin requirements in stressed market conditions may indeed lead to a higher demand for cash collateral, amplifying liquidity and volatility issues in other parts of the financial system. For example, some observers consider that the increase in haircuts that was applied to certain government bonds in cleared repo transactions during the most acute phases of the sovereign debt crisis of 2011 increased tensions on these sovereign debt markets[9]. Some studies have also suggested that the increase in variation margins on derivative contracts held by euro area insurance companies and pension funds at the outset of the Covid crisis contributed to significant outflows from euro-denominated money market funds (MMFs) used as sources of liquidity by these firms[10]. During that period, margin increases on the derivative positions held by investment funds amplified the liquidity issues that these funds were already facing due to significant redemptions, leading to sales of securities that had adverse impacts on the underlying markets[11].

EMIR includes a certain number of measures that aim to mitigate the effects of margin procyclicality (requirement for CCPs to monitor regularly the level of margins according to market conditions, anti-procyclicality (APC) margin measures…). These measures helped to alleviate the effects of recent market stresses, but also showed some limitations in terms of their level of granularity and the consistency of their implementation across the EU. An initiative was launched in 2022 by ESMA aiming to fine-tune these tools and improve their consistency. Work is also underway at the international level led by CPMI-IOSCO and the BCBS to review margining practices, following an assessment by the FSB of the March 2020 market turmoil.

6. A number of initiatives have been implemented to address the mismatch between the international dimension of derivative clearing and a supervisory approach that remains essentially local: on the regulatory front, with the PFMI (Principles for financial market infrastructures) international standards and on the supervisory front with the creation of global supervisory colleges.
7. See ESMA report of December 2021 – Assessment report under Article 25(2c) of EMIR.
8. The Commission has adopted CCP equivalence decisions for more than 20 jurisdictions and concerning more than 40 third-country CCPs – Source European Commission Communication – A path towards a stronger EU clearing system – 7 Dec 2022.
9. See "Repurchase agreements and systemic risk in the European sovereign debt market" HAL, 18 February 2020.
10. Together with bank deposits, repo agreements etc. See "Interconnectedness of derivatives markets and MMFs through insurance corporations and pension funds", ECB Financial Stability Review, November 2020.
11. See "The impact of derivatives collateralization on liquidity risk: evidence from the investment fund sector", ECB Working Paper Series N°2756 December 2022. Liquidity risk manifested itself in the March 2020 coronavirus related market turmoil, when market volatility and margin calls rose dramatically, including for non-bank financial intermediaries. Facing liquidity squeeze from both margin calls and redemptions, euro area investment funds sold securities worth almost € 300 billion in the first quarter of 2020, which amplified the adverse market dynamics. The report also notes that despite this episode and an increasing collateralization in derivative markets, investment funds' holdings of liquid assets continued to decline after March 2020 and reached the lowest level since 2013 at the end of 2020.

2.3 Challenges from energy and commodity derivative markets

Some challenges from energy and commodity derivative markets were brought to the forefront with the energy crisis triggered by the Russian invasion of Ukraine.

Commodity derivatives allow firms of the energy sector such as energy producers, suppliers and distributors to manage risks of volatile prices and offer long-term fixed price contracts to customers. Most of the trading in energy derivatives is conducted on regulated (futures) markets and is centrally cleared via CCPs established in the EU and regulated under EMIR[12]. In most cases, energy companies access CCPs via a clearing member, but some large energy companies access CCPs directly.

With the sharp rise in gas and electricity prices initiated in 2022, EU energy companies have been exposed to substantial margin increases and liquidity pressures. They have been required to post higher amounts of cash collateral to CCPs, as margin calls have risen in line with prices in order to guarantee the performance of derivative contracts, resulting in liquidity strains for these companies. ESMA's assessments also showed that in certain markets these liquidity issues led some energy companies to reduce hedging activities, potentially increasing risks in the market[13]. This prompted calls to review the rules governing margin requirements in the energy derivative markets and also for energy companies to enhance liquidity management in order to be in a position to meet margin calls in stressed conditions[14].

The impact of a possible energy price cap or market correction mechanism on CCP clearing is a further issue that is being assessed. A mechanism impacting price formation may indeed have negative implications for the energy futures market in terms of margin requirements and liquidity, according to some market stakeholders, potentially increasing risks in the market.

2.4 Emerging trends related to technology and climate change

Some new trends and impacts from technology and climate change are also emerging in the clearing space.

New technologies such as blockchain and artificial intelligence (AI) create potential opportunities and challenges for central clearing. First, the technologies underlying crypto and decentralised finance (DeFi) – *i.e.* blockchain, smart contracts, tokenisation… – and AI have the potential to improve significantly the efficiency and risk management of clearing activities *e.g.* with mechanisms allowing an immediate settlement of transactions or an automatic liquidation of positions, allowing a reduction of counterparty risk. These technologies could eventually change the value chain and the way clearing services are provided *e.g.* potentially integrating clearing with the trading and settlement layers or even doing away with the central counterparty function. The potential impacts of these evolutions in terms of price formation and of the ability of financial markets to absorb supply or demand shocks will however need considering in particular[15]. Cyber-risks, which may increase with more digitalisation of clearing activities, are another issue that is due to be addressed with the implementation of the Digital Operational Risk Act (DORA). Blockchain technology moreover supports the creation of new assets such as cryptoassets, related derivatives and tokenised assets, the clearing of which may produce new challenges for CCPs and their supervisors due to risk profiles that differ quite significantly from traditional financial instruments.

Climate change is a second trend that may impact CCPs in different ways over time. First in terms of physical risk to the operations of CCPs, their counterparties and service providers. Secondly in terms of the availability and adequacy of collateral. Thirdly, climate change could make it harder for CCPs to appropriately calibrate their risk models and identify possible future stress scenarios in a context where most models have a backward-looking approach to risk calibration based on historical data.

3. EMIR 2.2 review and assessment of third-country CCP risks

3.1 EMIR 2.2. review: changes for third-country and EU CCPs (2019)

A review of EMIR (EMIR 2.2) was adopted in 2019, focusing mainly on addressing the risks from the exposure of the EU to UK-based CCPs, following Brexit. EMIR 2.2 established a dedicated CCP Supervisory Committee (SC) within ESMA[16] in charge of supervising third-country CCPs (TC CCPs) that

12. See European Commission: Letter from DG FISMA to ESMA September 2022 – Response to the current level of margins and of excessive volatility in energy derivatives market.
13. See ESMA's response regarding the current level of margins and of excessive volatility in energy derivatives markets 22 September 2022.
14. In addition emergency measures were put in place in some Member States to alleviate market stress such as public guarantee schemes.
15. See "The future of clearing" Focus of the World Federation of Exchanges by Klaus Löber June 2022.
16. The CCP SC is composed of three independent members, the relevant national authorities and the national central banks of issue and reports to the ESMA Board of Supervisors.

are systemically relevant for the EU and enhancing supervisory convergence for EU-based CCPs.

For TC CCPs, EMIR 2.2 introduced a tiering of CCPs depending on their systemic importance for the financial stability of the EU and its member states. Non-systemic TC CCPs (Tier 1) are allowed to continue to provide services in the EU under the supervision of their home supervisors after being recognised by ESMA. Systemically important TC CCPs (Tier 2) have to comply with most EMIR requirements[17] and potentially additional requirements imposed by the relevant central banks of issue (CBI)[18] and are supervised by ESMA through the CCP SC. This is in effect a shared supervision between the UK and the EU authorities, which notably involves exchanges of information on the activities and risks of the CCPs concerned and the possibility for ESMA to conduct investigations and inspections if needed. To avoid an excessive burden on the CCPs potentially subject to a double set of rules, EMIR 2.2 introduced a concept of comparable compliance in Article 25, which is an equivalence assessment that is entity-based rather than jurisdiction based (as for traditional equivalence). In addition, ESMA can also propose to the European Commission, after having consulted the ESRB and the relevant CBIs, to not recognize in the EU a TC CCP or some of its clearing services that may be considered of 'substantial systemic importance' in the EU *i.e.* too systemically important to be located outside the EU.

For EU CCPs, in addition to national CCP supervisors who remain in charge of the supervision of the CCPs established in their jurisdiction, EMIR 2.2. introduced a more pan-European approach to supervision. The objective of the ESMA CCP Supervisory Committee is to promote supervisory convergence, bringing together in a single forum the different national competent authorities and central banks concerned by the supervision of EU CCPs. EMIR 2.2 has also strengthened the role of colleges of supervisors and central banks of issue in the supervision of CCPs.

3.2. Assessment of the challenges from UK-based clearing activities (2021)

In January 2021 the Commission set up a working group including representatives from the ECB, the ESAs and the ESRB to explore the opportunities and challenges from a potential transfer of derivative clearing activities from the UK to the EU. The discussions at the Working Group showed that a combination of different measures to improve the attractiveness of clearing, to encourage infrastructure development, and to reform supervisory arrangements were needed in the EU to build strong and attractive central clearing capacity in the years to come.

In parallel, ESMA conducted a comprehensive assessment of Tier 2 CCPs established in the UK and the risks they may pose to the financial stability of the EU and its member states. This assessment led to the identification of three clearing services considered to be systemically important for the EU, particularly in times of stress, due to the size of exposures of EU market participants, interconnections between these services and the EU and the lack of alternative services in the EU: interest rate derivatives denominated in euro and Polish zloty, short-term interest rate futures and credit default swaps denominated in euro[19].

ESMA did not recommend to derecognise these services or the CCPs providing them, considering that the costs for the EU would outweigh the benefits[20]. A non-recognition would indeed imply a range of costs and risks for EU counterparties including transfer costs, costs of breaking netting sets (reduced netting efficiencies, higher amounts of collateral…), potential additional costs and risks of a 'basis' developing *i.e.* a price difference between two CCPs offering clearing for the same product[21], significant competitive disadvantages for EU clearing members and risks related to the potential shift of EU clearing volume to another third-country. Potential benefits would only materialise if positions are transferred to EU CCPs and may include the reduction of dependencies on the UK and a facilitation of risk management (increased ability of the EU authorities to access information in a timely manner and to intervene effectively during a crisis situation) and resolution planning (early intervention powers to guard EU financial stability).

ESMA proposed instead measures to be considered by the EU institutions for reducing and mitigating the risks posed by these services. These include the implementation of appropriate incentives for reducing the exposure of EU participants to Tier 2 CCPs, the expansion of ESMA's supervisory and crisis management toolbox particularly regarding cross-border systemic risks and a revision of the framework for comparable compliance regarding Tier 2 CCPs[22].

17. Tier 2 CCPs need to comply with the prudential, organizational, conduct, reporting and interoperability requirements of EMI.
18. The CBI may for instance impose the submission of additional information, requirements to address temporary systemic liquidity risks, the opening of an overnight deposit account…
19. On 22 March 2022, ESMA amended the recognition decisions and tiering determination decisions in respect of the 3 recognised UK CCPs (ICE Clear Europe Ltd and LCH Ltd as Tier 2 CCPs and LME Clear Ltd as Tier 1 CCP) to extend them temporarily until 30 June 2025.
20. See ESMA, "Assessment report" under Article 25(2c) of EMIR of LCH Ltd and ICE Clear Europe Ltd, 16 December 2021.
21. Bases can develop between two CCPs if there is a different composition of market participants, with more or less directional portfolios, and different market flows across the two CCPs. Empirical data shows that bases change over time, can be volatile and are unpredictable. See ESMA assessment for further detail.
22. This includes the clarification that ESMA may retain supervisory powers over Tier 2 CCPs for EMIR requirements for which the Tier 2 CCP has been deemed comparably compliant.

4. Proposals for strengthening the EU clearing ecosystem (December 2022)

Following a consultation led in 2022 on proposals to increase clearing capacity in the EU and strengthen the supervision of clearing activities[23], the Commission made proposals to amend EMIR in 5 key areas, aiming to enhance the attractiveness of clearing in the EU and make EU CCPs more resilient. These proposals were published in the context of the action plan set out in December 2022 to complete the Capital Markets Union (CMU), taking into account the key role that CCPs play in supporting the development of safe and efficient capital markets.

These proposals are due to be assessed by the European Parliament and Council in the coming months, with the objective that they should be adopted before the end of the current legislature (Q2 2024) by the co-legislators. They will also be discussed during the April 2023 Eurofi Seminar in Stockholm and some initial views on these proposed expressed by a range of public and private sector representatives can be found in the April 2023 edition of the Eurofi Views Magazine.

4.1 Acceleration of procedures for approving new activities and simplification of equivalence assessments in low risk situations

CCPs need to be able to respond to developments in the markets and economic circumstances dynamically in order to contribute to financial stability and to maintain the competitiveness of EU CCPs. The industry has been complaining for many years about approval processes for launching new clearing activities and products in the market and implementing model changes considered to be unnecessarily long and burdensome[24], which increases costs and may put the EU at a disadvantage compared to other jurisdictions.

The introduction of new procedures and standardised applications that the authorities involved in EU CCP supervision should follow to approve new activities or services and changes in risk models has been proposed, with the objective to reduce the delay for obtaining approvals to a few weeks. A new shorter procedure for launching new activities and services that do not materially change the business model of a CCP will also be introduced. The aim is to encourage EU CCPs to broaden their product range in order to meet the demand of their clearing members and clients.

The Commission is also proposing to simplify equivalence assessments under EMIR when the risks related to clearing in a third country are particularly low, with a more proportionate equivalence framework and cooperation mechanisms with foreign supervisors better tailored to the magnitude of risks posed by CCPs located in third countries.

4.2 Requiring EU market participants to clear a portion of substantially systemic products through active accounts at EU CCPs

The Commission has been encouraging EU market participants since the UK's decision to leave the EU to reduce their excessive exposures to CCPs established in the UK in light of the potential risks in a stress scenario. Shifts of clearing activity to the EU have been observed in some areas such as euro-denominated repo, as well as the development of EU-based clearing activity by the private sector (*e.g.* with the creation of an alternative liquidity pool for euro denominated IRS by Eurex and the development of credit derivative swaps (CDS) clearing services by LCH SA), but the overall transfer of clearing activity to the EU has been limited so far.

In its December 2022 proposals, the Commission reasserted the objective of increasing clearing capacity in the EU and strengthening the EU clearing ecosystem, in order to alleviate the risks from an excessive exposure to UK CCPs and a possible interruption of the access of EU market participants to UK CCPs, while maintaining EU markets open to other jurisdictions. The legislative proposal recommends that EU market participants subject to a clearing obligation should be required to clear through "active" accounts at EU CCPs a portion (to be defined) of the products that have been identified by ESMA as of substantial systemic importance. To complement this measure, the amendment of the Capital Requirements and the Investment Firm Directives has also been proposed in order to enhance the monitoring and treatment of the concentration risk that may arise from exposures to CCPs[25].

4.3 Adjusting the UCITS and Solvency II Directives to reflect the risk reducing nature of central clearing

Banks benefit from a preferential prudential treatment when they clear at an authorized EU CCP or a recognised third-country CCP in order to acknowledge the reduction in counterparty credit risk that central clearing entails. This approach has not been fully

23. The objective is to ensure that the EU clearing ecosystem remains safe and resilient and support the CMU and open strategic autonomy objectives of the EU.

24. Currently, it can take up to 2 years for an EU CCP to get the supervisory approvals necessary to start offering a new clearing service.

25. The objectives of the measures proposed is to incentivize supervised entities (credit institutions and investment firms) to reduce excessive concentration risks by, for example, diversifying/scaling back their exposures. To the extent that a competent authority will consider that the actions taken by an entity it supervises are insufficient to reduce that risk, it will be able to impose supervisory measures.

mirrored in other pieces of financial legislation such as the rules on counterparty exposure limits for derivative transactions in the UCITS Directive, creating inconsistencies. The Commission has proposed amending the UCITS Directive and the money market fund (MMF) Regulation to better reflect the risk-mitigation role of CCPs authorised in the EU or recognised by ESMA.

A second issue highlighted in the December 2022 proposals concerns insurance companies wishing to become direct CCP members. At present under Solvency II, the CCP-related exposures of insurance companies wishing to become direct CCP members can be subject to higher capital requirements than where insurers act as indirect clearing participants. These higher capital requirements are a disincentive to using these new direct access models. This issue is due to be tackled in the context of the forthcoming revision of the relevant Solvency II Delegated Regulation[26].

4.4 Enhancing the cross-border supervision of EU CCPs

Developing the EU clearing ecosystem may lead to additional risks within the EU due to increased clearing volumes. In addition, recent market stresses (*e.g.* in the energy and MMF markets) have demonstrated the interdependencies among different types of economic actors in the clearing space and the externalities of clearing activities for the wider financial system.

A more holistic monitoring and control of clearing activities and interactions among market participants has been proposed to address these risks, as well as an improvement of the level of information on the relationships and interdependencies across the entire clearing chain and the liquidity issues that different market participants may experience due to margin increases.

The Commission also considers that the EU supervisory framework must be reinforced, to ensure the authorities work together effectively on the ground both at the national and EU levels, share knowledge and insights and develop a common supervisory culture, particularly to handle emergency situations, in the interest of the different stakeholders concerned. Building on the new supervisory and coordination roles of ESMA regarding CCPs in EMIR 2.2, the Commission communication proposes: i) establishing joint supervisory teams for certain tasks; ii) allowing ESMA, through its CCP Supervisory Committee, to coordinate common responses to emergency situations on the basis of up-to-date information; and (iii) facilitating the monitoring by EU authorities, such as the ESAs, ECB, ESRB and the SSM, of cross-border risks to the EU throughout the clearing chain.

4.5 Strengthening the framework for clearing commodity derivatives

Following the pressures on liquidity that some energy companies experienced in 2022 because of higher margin calls linked to rising energy prices, some emergency measures were proposed for energy derivatives, including (i) an increase of the threshold to € 4 billion, below which non-financial counterparties will not be subject to margin requirements on their OTC energy derivatives and (ii) a temporary broadening for one year of the list of eligible assets that CCPs may accept to cover their risks on energy derivatives markets; these may be extended *e.g.* to uncollateralized bank guarantees for non-financial companies (NFCs) acting as clearing members and to public guarantees for all types of counterparties[27].

In addition to these emergency measures, the Commission proposed increasing the transparency on margin models in order to allow all participants in the energy markets, including producers, suppliers and distributors, to get a better understanding of their potential liquidity needs when clearing centrally, particularly in situations of stress. Clearing members will moreover be required to explain to their clients how margin calls work and provide simulations under different scenarios building on the tools that EU CCPs provide to simulate the behaviour of margin models.

The legislative proposal amending EMIR also strengthens the requirements for non-financial firms participating in a CCP, in order to avoid that undue risks spill over to other clearing members. The proposal also takes into account ESMA's recommendations to amend the methodology to determine the clearing threshold, making it easier to implement and more predictable. It also requires ESMA to review and clarify the conditions for a transaction to be considered a hedge and therefore not count towards the clearing threshold.

26. Some observers have suggested that measures are also needed to support the direct access to CCPs of EU pension scheme arrangements that are due to come under a clearing obligation in June 2023. This could potentially increase liquidity in the EU market, but pension funds need to be able to convert their securities into cash in order to face margin calls. This requires a proper functioning of the repo market at all times at reasonable pricing conditions or the availability of other collateral transformation services. See Eurofi Summary Prague September 2022 "Strengthening EU clearing".

27. In its response to the Commission letter regarding the current level of margins and of excessive volatility in energy derivatives markets (22 September 2022), ESMA emphasized that any potential policy measures should avoid transferring risk from the energy sector into the financial sector and that a holistic view needs to be taken in terms of risks and costs. With this in mind, ESMA recommended clarifying the conditions under which different types of collateral can be accepted (EU bonds, commercial paper) and temporarily extending acceptable collateral to commercial bank guarantees backed by public entities and uncollateralized commercial bank guarantees under certain circumstances (see ESMA RTS Emergency measures on collateral requirements. 14 October 2022).

4.6 Further engaging the EU public authorities in the central clearing ecosystem

In order to increase clearing capacity in the EU, the Commission encourages in the legislative proposal public entities and authorities in the EU such as public debt management offices, which are currently exempted from EMIR derivative clearing requirements, to centrally clear their positions at EU CCPs, when the products sought are available.

Secondly, the Commission invites national public authorities to assess national accounting rules applying to hedging in order to remove or alleviate any obstacles to transferring exposures from third-country CCPs to EU CCPs and eliminate any uncertainties as to how certain national rules may apply.

Thirdly, the Eurosystem central banks are invited to address some operational issues that may hinder central clearing in the EU. A first issue is the operating hours of TARGET 2 which are considered to be too short, leading EU CCPs to call some margins late in the day in foreign currencies such as the US dollar rather than in EU currencies. This creates difficulties for CCPs that have to find ways to invest the US dollars received in the repo market and for clearing members and clients who need to have the necessary amounts of US dollars available to meet the margin calls. This could be a concern particularly in times of stress when CCP margin calls can occur late in the day and are of varying amounts. A further issue relates to central bank access policies for CCPs regarding deposit and liquidity facilities, which could be further harmonized across the Eurosystem.