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EMIR 3 (FOR AN ATTRACTIVE AND RESILIENT EU CLEARING)

Updated in March 2024

EMIR, which is the European translation of the G20 leaders' commitment made during the 2009 Pittsburgh Summit to enhance transparency on the derivatives market and mitigate the current risk generated by those transactions, has entered into force in August 2012.

Since then, EMIR has been reviewed two times:

- In June 2019, EMIR Refit¹ brought simplification and introduced a more proportionate approach for clearing obligations, reporting requirements, risk mitigation techniques, Trade Repositories registration and supervision
- While EMIR 2.2 (January 2020) was dedicated to CCPs' authorization and supervision with a specific focus on third country CCPs

EMIR 3, issued in December 2022, intends to *"make EU clearing services more attractive and resilient, supporting the EU's open strategic autonomy and preserving financial stability"*. The proposed amendment of EMIR goes hand in hand with the ones on Capital Requirement (directive and regulation), Investment Firms (directive), UCITS (directive) and Money Market Funds (regulation). The intention is to *"encourage financial institutions and investment firms respectively, as well as their competent authorities, to systematically address any excessive concentration risk that may arise from their exposures towards CCPs, in particular those systemically important third-country CCPs"*.

For legislative reasons, the amendments of the directives are in a dedicated directive, distinct from EMIR 3 since the latter is a regulation. Both drafts are part of a set of measures to further develop the EU's Capital Markets Union (CMU).

The "EMIRs" are built on four main pillars:

1. RISK MITIGATION for OTC derivatives contracts:

- The clearing obligation for all products considered sufficiently standardised
- For uncleared transactions, the rules have been strengthened to mitigate the counterparty risk (by setting an obligation of bilateral exchange of initial margin and variation margin) and the operational risk

2. TRANSPARENCY

- Obligation of reporting to a Derivatives Trade Repository
- Information to be provided

3. INFRASTRUCTURE

- More stringent requirements for clearing houses (CCPs)
- Establishment of a European legal framework for Trade Repositories

¹ The European Commission has established in 2012 the Regulatory Fitness and Performance programme (known as REFIT) aiming to make EU law simpler and to reduce the costs and burden of a regulation while still achieving intended benefits

4. THIRD COUNTRIES

- Third country equivalence
- Third country (TC) CCPs recognition

1. Overview

Since EMIR 3 aims at mitigating excessive exposures to third country CCPs and improve efficiency and attractiveness of the EU clearing markets, both EMIR Refit and EMIR 2.2 will be amended by EMIR 3 (see the table at the end of the document).

a. Key aspects of the Regulation

• Active accounts

THIRD COUNTRY
RISK MITIGATION

One of the objectives targeted by the EC is to reduce the exposure of EU clearing members to third country CCPs of systematically importance (those qualified Tier 2 by EMIR 2.2) and thus preserve the financial stability of the Union. For example, the EC pointed out the critical dependence on some services provided by CCPs in the UK (with a market share of more than 90% of euro-denominated derivatives) and concluded there was a need to:

- improve attractiveness of EU clearing
- encourage infrastructure development in the EU
- enhance supervisory arrangements in the EU

This in line with the ESMA's conclusions after its assessment of the two Tier 2 UK CCPs (LCH Ltd and ICE Clear Ltd). ESMA considered that the cost and consequences of a derecognition would be disproportionate in comparison with the benefits for the Union. For this reason, ESMA preferred measures aimed at limiting risks rather than questioning the recognition given to these CCPs:

- Incentives for reducing the size of EU exposures to Tier 2 CCPs
- Revising comparable compliance framework
- Expanding ESMA's supervisory and crisis management toolbox
- Enhancing cooperation with UK authorities on CCP recovery and resolution

THE ACTIVE ACCOUNT

Practically EMIR 3 introduces the notion of "active account". Financial and non-financial counterparties subject to the clearing obligation (FC+ and NFC+ in accordance with EMIR Refit) will be required to clear a portion of the products that have been identified by ESMA as of substantial systemic importance through active accounts at EU CCPs. According to the EC, *"roughly 60% of the EU clients of EU clearing members already have an account for clearing interest rate swaps at an EU CCP, and roughly 85% have one for credit default swaps"*².

SCOPE OF DERIVATIVES CONTRACTS

When assessing the two Tier 2 UK CCPs (LCH Ltd and ICE Clear Ltd), ESMA identified, based on its valuation methodology³, different scenarios that could impact financial stability in Europe; actually: the clearing offer on IRS in Euros and Polish Zlotys (LCH Ltd) and the clearing offers of CDS and STIR when they relate to Euro (ICE Clear Ltd). These are the products targeted by EMIR 3. The initial list will be amended in accordance with ESMA's new assessments.

PROPORTION OF ACTIVITY

The counterparty (FC+ or NFC+) is responsible to calculate its activities for these derivatives contracts at an EU CCP and report on an annual basis the result to the competent authorities of the related CCP. The calculation methodology as well as the proportion of activity to be on active accounts will be defined in a level 2 (delegated acts).

THE JOINT MONITORING MECHANISM (JMM)

Composed of representatives of ESMA, EBA, EIOPA, the EC, ESRB and ECB, the JMM will be responsible for monitoring the implementation of this new requirement.

² Page 9 of the EC's proposal

³https://www.esma.europa.eu/sites/default/files/library/methodology_for_assessing_a_tc_ccp_under_article_252c_of_emir_.pdf

IMPACT ON OTHER LEGAL TEXTS

The CRD-CRR (capital requirements) and the IFD (investment firms) are also impacted:

- Credit institutions and investment firms will be obliged to include in their risk management and monitoring process the concentration risk resulting from exposures to CCPs, considering the provisions relating to the active account
- Competent authorities will be able to require credit institutions and investment firms to reduce their exposures to a CCP in accordance with the obligation to the active account when they consider that the concentration risk is excessive.

• Information on clearing services

EMIR 3 inserts a new article that requires clearing members and clients that provide clearing services on OTC derivatives:

- to inform their clients on the possibility to clear these contracts at a European CCP
- to report each year to their competent authority a detailed scope of the activity they cleared at third country CCPs (recognized under article 25 of EMIR).

THIRD COUNTRY
TRANSPARENCY

• Clearing

RISK MITIGATION

EXEMPTION FOR PENSION SCHEME ARRANGEMENT (PSA)

EMIR 3 introduces an exemption from the clearing obligation where an EU Financial Counterparty or an EU Non-Financial Counterparty subject to this obligation (FC+ or NFC+) transacts with a PSA established in a third country which is exempted from the clearing obligation under its national law.

CLEARING THRESHOLDS (FC+/FC- & NFC+/NFC-) AND HEDGING EXEMPTIONS

EMIR 3 wants to reinforce ESMA's review including the scope of asset classes to be concerned. In particular, ESMA is encouraged to consider ESG criteria or crypto-related features.

POSITION TOWARDS THE THRESHOLDS (FC+/FC- & NFC+/NFC-)

EMIR 3 intends to clarify the rules for calculating the position towards the thresholds under article 4a (FC) and article 10 (NFC): only those derivative contracts that are not cleared at a CCP authorised under article 14 (EU CCPs) or recognised under article 25 (third country CCPs) should be included in the calculation.

FC		NFC	
In calculating the positions referred to in paragraph 1, the financial counterparty shall include all OTC derivative contracts that are not cleared in a CCP authorised under Article 14 or recognised under Article 25 , entered into by that financial counterparty or entered into by other entities within the group to which that financial counterparty belongs.		In calculating the positions referred to in paragraph 1, the non-financial counterparty shall include all the OTC derivative contracts that are not cleared in a CCP authorised under Article 14 or recognised under Article 25 , entered into by the non-financial counterparty which are not objectively measurable as reducing risks directly relating to the commercial activity or treasury financing	
FC+	FC-	NFC+	NFC-

• Intragroup transactions involving a third country entity

EMIR grants two exemptions to intragroup transactions, firstly from the clearing obligation and secondly from the margin requirements. When the transaction involved a third country entity, the exemptions apply only if an equivalence decision under article 13 of EMIR has been adopted.

Since the process to assess the equivalence takes time, ESMA has postponed (currently until the 30/06/2025) the obligation to clear / exchange margins in case there is no adopted equivalence.

EMIR 3 proposes to replace the need for an equivalence by a list of third countries for which an exemption should not be granted.

THIRD COUNTRY
RISK MITIGATION

The list will comprise:

- Those considered “high-risk third country” in accordance with the Directive 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing,
- Those listed in the Annex I of the Union list of non-cooperative jurisdictions for tax purposes.

- **Impacts on UCITS Directive (2009/65) and MMFR (2017/1131)**

In parallel with EMIR 3, the EC proposes to amend those two legal texts to better reflect the risk-mitigation role of CCPs authorised EU CCPs or recognised third country CCPs. Article 52 of the UCITS Directive is amended to eliminate counterparty risk limits for all derivative transactions if they are centrally cleared by a CCP that is authorised or recognised under Regulation (EU) No 648/2012. The same evolution is made in article 17 of MMFR. As regards UCITS, one can refer to the ESMA paper⁴ for more detail on the issue.

RISK MITIGATION

- **Third country (TC) CCPs**

EMIR 2.2 has introduced a notion of Tier 1 or Tier 2 TC CCPs. Tier 1 ones are those that are not systematically important or likely to be important for the financial stability of the Union or of one or more of its Member States. EMIR 2.2 also detailed the process for the recognition of TC CCPs. If there are additional conditions to be fulfilled for Tier 2 CCPs, there might be some too strict requirements for Tier 1 CCPs, for example the requirement in relation to the mechanism for the exchange of information between ESMA and the competent authorities of the third country, including access to all information requested by ESMA regarding CCPs authorised in the third country. Such obligation has conducted ESMA to withdraw the recognition of 6 Indian CCPs.

THIRD COUNTRY

INFRASTRUCTURE

EMIR 3 intends to have more proportionate cooperation arrangements that will be tailored depending on the jurisdiction. On the other hand, the requirements are reinforced for Tier 2 CCPs.

- **CCPs’ interoperability**

EMIR 3 clarify that CCPs should not be allowed to be clearing members of other CCPs nor accept to have other CCPs as clearing members or indirect clearing members (please refer to the ESRB document for any information on how links between CCPs could be set up).

INFRASTRUCTURE

- **Segregation**

EMIR 3 mandates ESMA to submit a report one year after its entry into force on “the possibility and feasibility to require the segregation of accounts across the clearing chain of non-financial and financial counterparties. The report shall be accompanied by a cost-benefit analysis”.

INFRASTRUCTURE

b. Other aspects

- **Reporting to Trade Repository – Intragroup exemption**

EMIR Refit granted an exemption of the mandatory reporting to transactions that were between two counterparties of the same group and for which at least one of the counterparties was a non-financial one (NFC). EMIR 3 removes this exemption on the grounds that it limits the ability of European bodies to clearly identify the risks taken by non-financial counterparties.

TRANSPARENCY

- **Clients’ information**

Clearing members and clients providing clearing services shall ensure transparency towards their clients.

TRANSPARENCY

⁴ [2015-880_esma_opinion_on_impact_of_emir_on_ucits.pdf \(europa.eu\)](#)

- **EU CCPs' authorisation**

INFRASTRUCTURE

SCOPE OF PRODUCTS

CCPs authorised to provide clearing services and activities on financial instruments may ask for an extension to non-financial instruments suitable for clearing.

AUTHORISATION / EXTENSION OF AUTHORISATION

EMIR 3 contains several measures to make the processes shorter, less complex, and more certain. In addition, EMIR introduces a "non-objection" procedure for the authorisation of additional services or activities when they do not increase the risks for the CCP. Moreover, the CCP may start clearing such additional financial / non-financial instruments before the decision of the CCP's competent authority.

WITHDRAWAL OF AUTHORISATION

Under EMIR 3 the competent authority will be required to consult ESMA and the members of the college prior any decision except in case of emergency.

- **EU CCPs' supervision**

INFRASTRUCTURE

THE JOINT SUPERVISORY TEAMS

EMIR 3 sets out Joint Supervisory Teams in order to increase the cooperations between authorities involved in the supervision of authorised CCPs (i.e. EU CCPs). Each CCP will have its JST, the tasks of which will include the provision of input to the CCP's competent authority within the context of the non-objection procedure, the support in establishing the frequency and depth of a CCP's review and evaluation as well as the participation to on-site inspections.

COOPERATION

More generally, EMIR 3 intends to further develop and strengthen the EU supervisory framework by increasing the cooperation and having authorities working together effectively on the ground, sharing knowledge and insights ...

ESMA

The role of ESMA is reinforced in EMIR 3, for example in the case of emergency situation or by issuing recommendations directly to a CCP's competent authorities.

- **Non Financial Counterparties (NFC)**

RISK MITIGATION

NFCs that become subject to the obligation to exchange collateral for OTC derivatives not cleared by a CCP (NFC+) will have 4 months to comply with the requirement. Contracts entered during the 4 months will be exempted from the obligation.

- **CCPs' membership**

INFRASTRUCTURE

If a CCP decides to onboard non-financial counterparties (NFC+), it should ensure that certain additional requirements on margin requirements and default funds are met. In addition, NFC+ are not allowed to offer client clearing services. Moreover, the CCP's competent authorities should report on a regular basis on the appropriateness of such membership.

c. Progress update and way forward:

- **Trilogue process**

November 2023: the EP has announced it has adopted its draft reports (published on the 6th of December 2023). On the same day the Council has adopted a mandate to start negotiations with the EP.

- **The European Systemic Risk Board (ESRB)'s opinion**

The ESRB has published an opinion on EMIR 3 (dated 20th of March 2023) in which it welcomes the EC's proposal and takes the opportunity to make some recommendations/comments.

For example:

- On the active account: the ESRB supports the limitation to those products identified by ESMA and recognises it is important to not undermine the competitiveness of the EU but suggests some amendments to ensure more efficiency
- On Data: the ESRB considers there is still substantial quality issues in the data reported by CCPs and large banking groups
- On the non-objection procedure: it should apply where settlement in a new EU currency would be added to a class of financial instruments already covered by the CCP's authorisation
- The Joint Monitoring Mechanism: there should be clarification on the intersection between the JMM and the existing supervisory framework.

In a letter sent (on the 4th of October 2023) to the EC, the EP and the Council, the ESRB pursues its contribution to the reflexion on the future active account, pointing out the dependency on the types of trades and on the thresholds applied. In addition, the ESRB considers that the active account would not be sufficient to address all the risks identified by the ESRB.

- **The industry**

Trade associations have published a joint letter requesting for the removal of the active account requirement (September 2023)

- **The future final text**

A political agreement has been reached on the 7th of February 2024.

Main elements of the agreement (extract from the Council's press release):

- The Council and Parliament ensured that in practice it is feasible for supervisory authorities to apply streamlined supervisory processes, such as authorisation and validation procedures.
- The provisional agreement strengthens cooperation, coordination and information sharing among supervisors and ESMA, while ensuring an appropriate division of tasks between national authorities and ESMA.
- The agreement also strengthens the role of ESMA providing it with a coordination role in emergency situations, while providing clarity that ultimate decision making powers are the responsibility of the national competent authorities.
- ESMA will also take the role of co-chair of supervisory colleges together with the relevant national competent authorities, who will keep ultimate decision making powers. Furthermore, ESMA will be informed about and may request to be invited to on-site examinations and provide opinions in an extended range of areas.
- The provisional agreement sets a solid active account requirement (AAR) that will require certain financial and non-financial counterparties to have an account at an EU CCP, which includes operational elements such as the ability to handle the counterparty's transactions at short notice if need be and activity elements so that the account is effectively used.
- This is ensured by a number of requirements, which have to be fulfilled by these accounts, including requirements for counterparties above a certain threshold to clear trades in the most relevant sub-categories of derivatives of substantial systemic importance defined in terms of class of derivative, size and maturity. Furthermore, a Joint Monitoring Mechanism is created to keep track of this new requirement.

2. Reference text(s)

- [ESMA's assessment of the two Tier 2 UK CCP \(Dec 2021\)](#)
- [EMIR 3 EC's proposal](#)
- [A path towards a stronger EU clearing system \(EC\)](#)
- [Summary of the impact assessment](#)
- [More on derivatives](#)
- [CMU press release](#)
- [ESRB CCPs interoperability arrangements](#)
- [Econ draft report](#)
- [Council progress report](#)
- [Joint letter](#)

- [ESRB letter to the EC](#)
- [ESRB letter to the Parliament](#)
- [ESRB letter to the Council](#)
- [EP draft report \(regulation\)](#)
- [EP draft report \(directive\)](#)
- [Final compromise regulation](#)
- [Final compromise directive](#)

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