

# Guidelines and Recommendations

Guidelines and Recommendations for establishing consistent, efficient and effective assessments of interoperability arrangements





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## **I. Scope**

### **Who?**

1. These Guidelines and Recommendations apply to national competent authorities (NCAs).

### **What?**

2. The Guidelines and Recommendations define what NCAs should analyse in assessing an interoperability arrangement and therefore on what aspects of the interoperable arrangement the relevant CCPs will need to focus their attention.
3. The Guidelines and Recommendations do not introduce new requirements for CCPs in addition to the ones specified in EMIR or the relevant technical standards. However, they specify how those requirements should be met for the purpose of establishing robust and stable interoperability arrangements.
4. The Guidelines and Recommendations focus on the risks that might arise from interoperability arrangements and outline the areas on which CCPs should focus, and which NCAs should verify, to mitigate those risks.

### **When?**

5. These Guidelines and Recommendations apply from 10-06-2013.

## **II. Purpose**

6. The objective of these Guidelines and Recommendations is to improve the rigor and uniformity of standards applied in the assessments of interoperability arrangements.

## **III. Compliance and reporting obligations**

### **Status of the guidelines**

7. This document contains General Guidelines and Recommendations and Detailed Guidelines and Recommendations. Both types are Guidelines and Recommendations issued under Article

16 of the ESMA Regulation<sup>1</sup>. In accordance with Article 16(3) of the ESMA Regulation NCAs must make every effort to comply with Guidelines and Recommendations.

8. NCAs to whom the Guidelines and Recommendations apply should comply by incorporating them into their supervisory practices.

### **Reporting requirements**

9. NCAs to whom these Guidelines and Recommendations apply must notify ESMA whether they comply or intend to comply with the Guidelines and Recommendations, with reasons for non-compliance, within two months of the date of publication by ESMA to [post-trading@esma.europa.eu](mailto:post-trading@esma.europa.eu). In the absence of a response by this deadline, NCAs will be considered as non-compliant. A template for notifications is available from the ESMA website.

## **IV. Guidelines and Recommendations for establishing consistent, efficient and effective assessments of interoperability arrangements**

10. Considering the requirements for CCPs entering into an interoperability arrangement as set out in Articles 51, 52 and 53 of the Regulation, ESMA proposes that NCAs, when reviewing an interoperability proposal pursuant to Article 54 of the Regulation, assess the application against the criteria set out in the Guidelines and Recommendations below.

### **GUIDELINE AND RECOMMENDATION ONE: LEGAL RISK**

(Article 52(1)(a) and (b) of Regulation (EU) No 648/2012)

#### *General Guideline and Recommendation 1*

A NCA should assess that the interoperability arrangement is clearly defined, transparent, valid and enforceable in all relevant jurisdictions and also that a CCP has put in place a framework to assess these factors before entering into an interoperability arrangement and on a regular basis.

#### *Detailed Guidelines and Recommendations*

##### **a) Documentation**

In applying general Guideline and Recommendation 1, NCAs should at least take into account that the documentation:

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<sup>1</sup> Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.

- i. Clearly identifies, in a form that is binding, the rights and obligations of the CCPs under the interoperability arrangement.
- ii. Is compatible with the risk mitigation processes of the CCP.
- iii. Establishes a process for regular review of the documentation, which ensures that the documentation remains appropriate and defines the responsibilities of the CCPs in that process.
- iv. Establishes a process to consult the risk committee and the clearing members where the establishment of, or any change to, the interoperable arrangement is likely to have a material impact on the risks to which the CCP is exposed, and to inform the clearing members where the establishment of, or any change to, the interoperable arrangement may have an impact on their operations.
- v. Clearly indicates the process and the persons responsible for monitoring and ensuring the functioning of the interoperability arrangement.
- vi. Clearly defines the dispute resolution mechanism for disputes arising from the interoperability arrangement.
- vii. Clearly defines the conditions and procedure for termination of the interoperability arrangement.

## **b) Legal analysis**

When applying general Guideline and Recommendation 1, NCAs should at least take into account the following:

- i. That the CCP has assessed with a high degree of confidence that the netting arrangements between the interoperating CCPs are valid and enforceable.
- ii. That the CCP has assessed with a high degree of confidence that its rules and procedures concerning the moment of entry of transfer orders into its systems and the moment of irrevocability have been defined in accordance with Article 52(1) of the Regulation.
- iii. That the CCP has assessed with a high degree of confidence the potential for cross-border legal issues to arise as a result of its participation in the interoperable arrangement, in particular with regard to its default procedures and the enforceability of collateral arrangements.
- iv. That the CCP has assessed with a high degree of confidence that its procedures for the management of the default of the interoperable CCP are valid and enforceable.
- v. That the CCP has a high degree of confidence regarding the enforceability of its default rules against the interoperable CCPs and regarding the viability of its interoperability procedures.

## **GUIDELINE AND RECOMMENDATION TWO: OPEN AND FAIR ACCESS**

(Article 51(2) and (3) of Regulation (EU) No 648/2012)

### *General Guideline and Recommendation 2*

A NCA should assess that the interoperability arrangement ensures non-discriminatory access and that denial or restrictions on entering into an interoperability arrangement are based only on risk grounds.

#### *Detailed Guidelines and Recommendations*

##### **a) Documentation**

In applying general Guideline and Recommendation 2, NCAs should at least take into account that the documentation:

- i. Governing the interoperability arrangement does not contain any provision that restricts or creates obstacles for the establishment or future extension of the interoperability arrangement to other CCPs, other than on duly justified risk grounds.
- ii. Governing the interoperability arrangement does not unduly restrict the termination of the interoperability arrangement where one of the interoperating CCPs considers it necessary to terminate it on duly justified risk grounds. In such circumstances, the CCP deciding to terminate the interoperability arrangement needs to provide adequate justification to its NCA of its reasons to terminate the arrangement and provide clearing members, trading platforms served by the CCP and other interoperable CCPs, where appropriate, with as much notice as possible.

### **GUIDELINE AND RECOMMENDATION THREE: IDENTIFICATION, MONITORING AND MANAGEMENT OF RISKS**

(Article 52(1)(a), (b) and (c) and Article 52(2) of Regulation (EU) No 648/2012)

#### *General Guideline and Recommendation 3*

A NCA should assess that a CCP has put in place a general framework to identify, monitor and manage, before entering into an interoperability arrangement and on a regular basis, the potential risks arising from the interoperability arrangement.

#### *Detailed Guidelines and Recommendations*

##### **a) General policies, procedures and systems**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. That the interoperability arrangement does not impact on the compliance by the CCPs participating in the arrangement with the requirements to which they are subject under the Regulation and relevant technical standards or equivalent regulations in third countries. In this respect, these requirements should be met by each CCP on a standalone basis, in particular with reference to prefunded financial resources including margins.

- ii. That the CCPs exchange the necessary information on their operations, including, where relevant, the potential reliance on third parties as critical service providers, enabling each CCP to perform effective periodic assessments and to identify, monitor, and mitigate any new or increased risk, interdependencies or spill over effects that may arise from the interoperability arrangement.
- iii. That there is a process for the regular review of the CCP's risk management framework following the assessment in point (ii).
- iv. That there is a process for agreeing between the interoperable CCPs any changes to the interoperability arrangement and for resolving disputes.
- v. That there is a process for:
  - a. informing the interoperable CCPs of any change to the rules of the CCP; and
  - b. agreeing between the interoperable CCPs any changes to the rules of one CCP that directly impacts the interoperability arrangement.
- vi. In case of interoperability arrangements involving three or more CCPs, that the CCP has defined policies, procedures and systems to identify, monitor, assess and mitigate the risks arising from the collective arrangements and the rights and obligations of the different interoperable CCPs.
- vii. That the CCP's operational arrangements, processing capacity and risk management arrangements are sufficiently scalable and reliable for both the current and projected peak volumes of activity processed through the interoperable link and the number of CCPs involved in the interoperability arrangement.
- viii. That the communication arrangements between the interoperable CCPs ensure timely, reliable and secure communication.
- ix. That the CCP's default management procedures are designed to ensure that the management of a default of a clearing member of one CCP does not affect the operations of the interoperable CCPs or expose them to additional risks.
- x. That the CCP has assessed the need for specific default management procedures in view of the interoperability arrangement.
- xi. That the procedure for the termination of the interoperability arrangement by any of the interoperable CCPs is clear and transparent and will result in termination in an orderly manner that does not unduly expose the interoperable CCPs to additional risks.

## **b) Prudential requirements**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. That financial risks, including custody risks, arising from the interoperability arrangement are identified, monitored, assessed and mitigated with the same rigour as the CCP's exposures arising from its clearing members.
- ii. That the CCP has adequate processes, procedures and risk models, including methodologies for stress testing, to adequately forecast its financial exposures and liquidity needs arising from the interoperability arrangement
- iii. That the CCP has assessed, collected or has access to, the required inter-CCP resources necessary to cover credit and liquidity risk arising from the interoperable arrangement, including in extreme but plausible market conditions.
- iv. That the CCP has identified any risks arising from the interval between inter-CCP margin calls and the availability of the relevant collateral.

- v. That the interoperable CCPs are not allowed to contribute to each other's default funds or other financial resources as defined in Article 43 of the Regulation.

### **c) Interoperable CCP default**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. The CCP's potential exposures arising from uncovered credit losses if an interoperable CCP's default waterfall has been exhausted.
- ii. The degree to which the portability of positions from the defaulting CCP to a non-defaulting CCP or a default fund of the interoperable CCP, which is dedicated to covering the exposures arising from financial instruments cleared through the interoperable arrangement, would contribute to the lowering of the inter-CCPs exposures.
- iii. Ensuring that risks introduced by the interoperability arrangement are disclosed to the clearing members in line with the Article 38(2) of the Regulation and Article 10 of Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 with regard to regulatory technical standards on requirements for central counterparties).
- iv. Where more than two CCPs participate in an interoperability agreement, the risks of the collective interoperability arrangement.
- v. The likely liquidity needs resulting from the interoperability arrangement such as in the case of an inter-CCP margin call not being met.

### **d) Different risk-management models**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. That the CCP has a process for regularly assessing differences between the risk-management frameworks, if any, of the interoperating CCPs, identifying any risks that may arise from the use of such different models or controls, including assessment of the results of stress tests and the testing of default procedures, and has arrangements in place for mitigating those risks.
- ii. That following the assessment in point (i), there should be a process for interoperable CCPs to review their risk management frameworks and consider possible actions, including the case for further convergence of the risk management frameworks.

### **e) Risk profile and membership criteria**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. That the CCP has assessed the risk profile of each interoperating CCP, including any risks that may arise from its membership policies, to ascertain that the interoperability arrangement does not result in a weakening of the CCP's overall risk management framework.
- ii. That the CCP has policies, procedures and systems to regularly monitor, assess and mitigate any risk arising from interdependencies, including from entities or groups of entities acting

as clearing members or providers of essential services to one or more interoperable CCP. In this respect, the concentration limits established by each CCP should be reviewed to ensure they remain appropriate in light of the interoperability arrangement, in particular if the arrangement gives rise to higher risks of interdependencies.

#### **f) Exposure management**

In applying general Guideline and Recommendation 3, NCAs should at least take into account the following:

- i. That the CCP has identified how it will cover exposures originating from the interoperability arrangement, including:
  - a. how it will calculate margin pursuant to Article 41 of the Regulation and Chapter VI of Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 with regard to regulatory technical standards on requirements for central counterparties.
  - b. how it will meet exposures following the default of an interoperable CCP without reducing the CCP's ability to fulfil its obligations to its own clearing members.
  - c. the assumptions for the determination and exchange of inter-CCPs margins. This should include a detailed explanation to the NCAs of the differences, if any, between the risk management parameters applied to the inter-CCP exposures as opposed to the ones applied to the clearing members.
- ii. That the CCP has put in place risk management tools, such as margin or default fund policies, to address any weakening of the CCP's overall risk management framework due to the interoperability arrangement.
- iii. That the CCP has put in place arrangements, which are transparent to its clearing members, to meet exposures arising from the interoperability arrangement, including in extreme but plausible market conditions.

### **GUIDELINE AND RECOMMENDATION FOUR: DEPOSIT OF COLLATERAL**

(Article 53(3) of Regulation (EU) No 648/2012)

#### *General Guideline and Recommendation*

1. A NCA should assess that an interoperable CCP deposits collateral in a way that it is protected from the default of any interoperable CCPs.

### **GUIDELINE AND RECOMMENDATION FIVE: COOPERATION BETWEEN NCAS**

(Article 54(2) of Regulation (EU) No 648/2012)

#### *General Guideline and Recommendation*

1. Without prejudice to the authorisation procedure outlined in Article 17 of the Regulation, the NCAs responsible for the assessment of the interoperability arrangement should closely co-

operate with each other during the assessment phase. This includes sharing information throughout the process and sharing their respective risk assessment reports before they are finalised and submitted to the respective colleges in line with the procedure set out in Article 17 of the Regulation. Without prejudice to the college arrangements under Article 18 of the Regulation, the NCAs responsible for supervision of the interoperable CCPs should closely cooperate with each other on a regular basis.

2. Where the interoperability arrangement is between a CCP authorised under Article 17 of the Regulation and a CCP recognised under Article 25 of the Regulation, there should be arrangements for cooperation between the NCA and the relevant third-country authority in order to respect the provisions in paragraph 1 of this Guideline and Recommendation. The establishment of the relevant arrangements may be facilitated through the cooperation arrangement between ESMA and the third-country competent authority, as established in accordance with Article 25(7) of the Regulation.