
EACH Position – MISP Settlement Finality Regulation (SFR): Issues and EACH proposals

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Introduction

The European Association of CCP Clearing Houses (EACH) represents the interests of Central Counterparties (CCPs) in Europe since 1992. CCPs are financial market infrastructures that significantly contribute to safer, more efficient and transparent global financial markets. EACH currently has 19 members from 14 different European countries. EACH is registered in the European Union Transparency Register with number 36897011311-96.

With this paper, EACH Members would like to put forward our views on the European Commission proposal for a regulation on settlement finality and repealing Directive 98/26/EC and amending Directive 2002/47/EC on financial collateral arrangements¹.

EACH Members support the European Commission's intention to harmonise the settlement finality framework, which is consistent with the wider goals of the Savings and Investment Union of addressing regulatory fragmentation.

Issues identified and EACH proposals

Issue #1 – Increased complexity and granularity

Article 3(2)

The designating authority of the Member State whose law governs the system may designate the system, where at least one of its participants has its head office in that Member State.

Article 4(2)

The application shall be immediately shared with all of the following:

- (a) the designating authority;*
- (b) where applicable, the national competent authority;*
- (c) ESMA;*
- (d) EBA for systems operating transfer orders set out in Article 2(1), point (20)(a);*
- (e) The ESCB.*

Article 5(1)(b)

A designating authority shall designate a system in accordance with Article 3, only where the designating authority is satisfied that all of the following conditions are fulfilled:

[...]

- (b) at least one of the participants;*

[...]

Article 7(2)

A system operator of a designated system may accept a system member to the system only where that member meets all of the following conditions:

- (a) it has the capacity and ability to meet the obligations arising from its participation in the system;*
- (b) it has the capacity and ability to mitigate the risks resulting from its participation in the system;*

¹ https://eur-lex.europa.eu/resource.html?uri=cellar:83376982-d0ff-11f0-8da2-01aa75ed71a1.0001.02/DOC_1&format=PDF

(c) it complies with the rules of the system.

A system operator of a designated system shall establish admission criteria, differentiating per type of participant where relevant. Such admission criteria shall be non-discriminatory, transparent and objective to ensure fair and open access to the designated system.

A system operator of a designated system shall ensure that the system members comply with the conditions set out in the first subparagraph on an ongoing basis and shall have timely access to the information relevant for such assessment.

Article 8(2)

The system operator shall notify, without undue delay, to the designating authority of any of the following:

(a) any material changes that affect or may affect the system operator's compliance, and that of the system it operates, with the provisions of this Regulation;

(b) any changes to the list of information provided for in Article 6(2), points (a) to (g).

Article 9(2)

[...] A designating authority shall only decide to withdraw the designation of a system after it has informed the national competent authority and requested an opinion on the appropriateness of withdrawing the designation. The opinion shall be requested from ESMA and the ESCB for the withdrawal of the designation for securities settlement systems and clearing systems, or from EBA and the ESCB, for the withdrawal of the designation for payment systems.

Article 21(3) and (4)

3. ESMA may, in close cooperation with the ESCB, for clearing and securities settlement systems not operated by a CSD, and taking into account the specificities of different types of systems, and the mechanics of those systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]

4. EBA may, in close cooperation with the ESCB, and taking into account the specificities of different types of payments systems and the mechanics of the systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]

Background

- **Articles 3(2) and 5(1)(b)** could be problematic for systems that do not necessarily have many participants in their Member State and provide services on a pan-European level. EACH Members question this provision that conditions the ability of the designating authority of the Member State whose law governs the system to designate the system on the system having at least one participant also based in that Member State.
- **Article 4(2)** increases complexity by increasing the number of stakeholders in the procedure for granting and refusing designation.
- **Article 7** establishes participation requirements for system participants that, while overlapping with existing Regulation (EU) No 648/2012 (EMIR)² requirements, could still require CCPs to amend their rules and procedures to ensure compliance.
- **Article 9** withdrawal involves NCA, ESMA, EBA and ESCB, increasing complexity by increasing number of stakeholders in the process.

² <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32012R0648>

- **Article 21(3) and (4)** gives ESMA and the EBA, respectively, the optional mandate to develop RTS to provide further granularity. EACH questions whether it is necessary or helpful to have such granular requirements. Please see EACH Proposal #18.

EACH Proposal #1 – Promoting simplification

- EACH Members suggest **addressing the issues described above** in order not to create unnecessary complications and compliance burden.

Issue #2 – Re-authorisation of current designated systems

Article 3(1)

Where an undertaking operates or intends to operate a system governed by the law of a Member State, such a system operator may apply for that system to be designated in accordance with the procedure laid down in Article 4, as a system in the Union to which the settlement finality rules laid down in Articles 17 to 25 apply. [...]

A system operator referred to in paragraph 1 that, to a limited extent, offers the settlement, clearing or execution of instructions related to instruments other than those referred to in Article 2(1), point (20)(b), may request that the settlement finality rules set out in Articles 17 to 25 also apply in relation to such instruments. The designating authority may allow such instructions to be considered transfer orders when it considers that such a designation is warranted on grounds of systemic risk.

Article 8(2)

The system operator shall notify, without undue delay, to the designating authority of any of the following:

(a) any material changes that affect or may affect the system operator's compliance, and that of the system it operates, with the provisions of this Regulation;

(b) any changes to the list of information provided for in Article 6(2), points (a) to (g).

Background

- **Lack of alignment with EMIR – Article 3(1)** establishes that “A system operator referred to in paragraph 1 that, **to a limited extent**, offers the settlement, clearing or execution of instructions related to instruments other than those referred to in Article 2(1), point (20)(b) [...]”. With regard to non-financial instruments, it is crucial to ensure alignment with EMIR. Regulation (EU) 2024/2987 (EMIR 3)³ clarifies that the authorisation of a CCP can extend to the clearing of non-financial instruments (see EMIR Articles 14(3), 15(1), and 17(4)). EMIR does not provide for a restriction that a CCP may only offer clearing of non-financial instruments “to a limited extent.”
- **Lack of a grandfathering clause – Article 8(2)(b)** requires system operators to notify the designating authority of any changes to the list of information provided for in Article 6(2), points (a) to (g). Accordingly, where system operators extend the scope of eligible participants or the common rules and standardised procedures of the system in response to the SFR, the designating authority will have full visibility thereof. Potential issues can be addressed without the need of formal re-authorisation. Another issue arises when the authorisation might need an extension, in particular with regard

³ https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202402987

to the inclusion of non-financial instruments (Article 3(1), second subparagraph). But also in this case, there should not be a requirement to apply for designation “from scratch”.

EACH proposal #2 – Ensuring alignment with EMIR

- In order to better align with the provisions included in EMIR, **the restriction in Article 3(1) should be deleted.**
- Reference to non-financial instruments should also be **included in SFR Article 19** to align with the intended wider scope of the SFR and EMIR 3.
- Furthermore, it should be ensured that the SFR, regarding the **scope of inclusion of non-financial instruments**, automatically **follows the scope of the CCP’s authorisation under EMIR.** When a CCP clears non-financial instruments, protection under the SFR would appear to be always *“warranted on grounds of systemic risk”* which is the decisive element under Article 3(1), second subparagraph. That is of particular relevance for CCPs clearing energy spot markets.

EACH Proposal #3 –Grandfathering clause for already authorised designated systems

- EACH Members consider crucial to **include a grandfathering clause** specifying that EU and third-country systems that already benefit from settlement finality protection **do not need to re-apply for designation or registration.** As drafted, and due to the absence of an explicit grandfathering clause or automatic carry-over for systems already designated under the existing SFD framework, **SFR Articles 3 and 12** would require currently designated or registered systems to apply again for designation or registration. Such re-authorisation process would impose a significant and unnecessarily burden for current designated systems, and would not bring any added value to either operators or competent authorities. It would also duplicate assessments that have already demonstrated the system’s robustness and compliance with stringent requirements.
- Such duplication does not generate legal certainty or financial stability for central counterparties. On the contrary, it **risks reducing legal certainty during the transition period by creating avoidable uncertainty** for all system participants and diverting resources from ongoing risk management and stability-enhancing functions. To preserve continuity and strengthen legal certainty, we therefore recommend **automatic grandfathering of existing designations** or, at minimum, a significantly simplified and non-duplicative recognition procedure for already designated systems.

EACH Proposal #4 – Maintain optionality of system designation

- EACH Members **support the optionality included in Article 3(1)**, which establishes that *“Where an undertaking operates or intends to operate a system governed by the law of a Member State, such a system operator **may** apply for that system to be designated in accordance with the procedure [...]”*.

Issue #3 – Third-country systems and participants

Article 1(2)

This Regulation also lays down requirements for the registration of third-country systems in one or several Member States in order to enable institutions established in those Member States, which participate in those third-country systems, to benefit from the extension of the insolvency protection provided for in Articles 17, 19, 22(1), 23, 24 and 25(1)⁴ to transfer orders entered into in such third-country systems.

In the case of an insolvency of a member of such a system, transfer orders entered by that member shall be protected where both the following conditions are met:

- a) the member participates in a registered system as defined in Article 2(1), point (9);*
- b) the member is an institution as defined in Article 2(1), point (10)(a)(i) to (iv) and (b), established in the Member State which has registered that system under Article 12.*

Background

- **Limitation of insolvency protection** – The provisions that will newly expressly apply to third-country systems as a matter of EU law are warmly welcomed as one of the most important proposed changes. However, SFR Article 1(2) limits insolvency protection in third country systems to “institutions”. This is a narrower category than the “participants” covered in EU systems and would, for example, seem to exclude CSDs which are not also credit institutions. The same provision is also very concerning because, as an initial scoping provision, it implies that the Regulation only applies to protect EU participants (so, by implication, not third-country system operators) from insolvency law challenges. This seems to be either in error or an under-statement of other provisions of the draft regulation. In this regard, Article 1(2) is inconsistent with the operative provisions of Articles 17, 19, 23, 24 and 25, all of which apply expressly to third country system operators and would appear to protect them from insolvency law challenges.
- **Unlevel playing field for insolvency law carve-outs** – SFR inconsistently applies insolvency protections to third-country systems. For example, Articles 17, 19, 23, 24 and 25 explicitly apply to third-country systems as to designated systems. However, Articles 18(1) (moment of entry) and 21(1) (final settlement) do not seem to apply to registered systems, despite the protections set out in these sections being fundamental to settlement finality. Article 20 (irrevocability) also omits third-country systems. This inconsistency is noteworthy because Article 14(d) *requires* third-country systems to define moments of entry, irrevocability, and final settlement by cross-reference to Articles 18, 20 and 21. A possible consequence of the current drafting is therefore to impose compliance burdens on third country CCPs to comply with the SFR framework, without providing any related benefits in terms of finality.
- **Protecting third-country CCPs under the SFRs, not just their EU participants, is critical** – System operators and especially CCPs are the entities who most need to rely upon the insolvency carve-outs in the current SFD framework, as well as the proposed SFR framework, in order for this to be effective and to promote financial stability. We

⁴ Art. 17: Netting and transfer order; Art. 18: Moment of entry of a transfer order into a designated system; Art. 20: The moment of irrevocability of transfer orders; Art. 21: Final settlement; Art. 22: The moment of opening of insolvency; Art. 24: Law governing the rights and obligations of participants; Art. 25: Collateral security

are concerned that the omission of appropriate references to third-country systems in Articles 1(2), 18, 20 and 21 could mean that insolvency practitioners appointed over EU participants might be incentivised to:

- ignore or challenge transfer orders processed through third-country systems;
- take actions seeking clawback from innocent participants ;
- sue system operators in respect of completed or supposedly irrevocable settlements;
- challenge the use of margin, default fund or other collateral by system operators.

We note that EMIR Article 48(4) requires CCPs to verify that their default rules are enforceable. Article 5 of Commission Delegated Regulation (EU) No 153/2013⁵ requires CCPs to take various compliance steps in this regard, including identifying and analysing potential conflicts of law issues, as well as analysing the soundness of their rules and contractual arrangements. These provisions apply to third-country recognised CCPs pursuant to EMIR Article 25, either on a direct applicability (tier 2) or comparability (tier 1) basis. For this reason, CCPs and CSDs must obtain legal opinions on the enforceability of their rules, including on an insolvency, under the jurisdiction of each clearing member or direct participant. Third-country CCPs and CSDs seek such legal opinions in respect of EU clearing members and need “clean” opinions in order to be able to provide access. It is therefore crucial that EU laws support third country systems such as CCPs having finality to their transfer orders, as a matter of the insolvency laws of member states.

EACH proposal #5 – Align the scope of insolvency protections for EU and third-country systems

- As mentioned above, SFR Article 1(2) limits insolvency protection in third country systems to “institutions”, which is a narrower category than the “participants” covered in EU systems. For consistency, **both provisions should refer to “participants”**.
- **Article 1(2) should also clarify as a matter of scope that the operative insolvency provisions of the SFR apply to system operators** as well as participants (consistent with Articles 17, 19, 23, 24 and 25, to avoid the possibility of unhelpful purposive interpretations to the contrary).
- **Articles 18, 20 and 21 should be expanded so as to apply to third country systems.** In a major step forwards, it is proposed that most of protections of the SFR will apply to third-country systems, namely:
 - Article 17 – enforceability of transfer orders and close out netting;
 - Article 19 – margin and default fund can be applied by system operator;
 - Article 22 – moment of opening of insolvency proceedings;
 - Article 23 – no retroactive events;
 - Article 24 – law governing rights of participants; and
 - Article 25(1) – enforceability of collateral security.

EACH Members also would like to receive clarifications on why Articles 18(1) (moment of entry of transfer order) and 21(1) (finality of transfer orders) are omitted and therefore not applied to third-country systems.

⁵ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013R0153>

Issue #4 – Participants and indirect participants

Article 1(3)

The Regulation applies to:

- a) *any system⁶ as defined in Article 2(1), point (1);*
- b) *any participant⁷ as defined in Article 2(1), point (15);*
- c) *a collateral security, as referred to in Article 25, provided in connection with and in relation to any of the following:*
 - i. *participation in a system;*
 - ii. *operations of the central banks of the Member States or the European Central Bank in the context of their function as central banks.*

Article 7(1)

[...]

A Member State may, in exceptional circumstances and for the purposes of this Regulation, admit an indirect participant as participant where the indirect participant is known to the system operator and the participants of the system, and where that is warranted on the grounds of systemic risk. That possibility shall, however, not limit the responsibility of the participant through which the indirect participant passes transfer orders to the designated system.

Background

- **Lack of recognition of indirect participants** – Currently, Member States have their own systems to recognise the systemic importance of an indirect participant. In such context, CCPs often need to request a legal opinion before accepting an indirect participant, which results in more costly and complex onboarding procedures. EACH Members therefore suggest further broadening of the scope of application to include indirect participants
- **Risk of double regulation** – The requirement on system operators to monitor compliance by system members with participation requirements (Article 7) would lead to a double regulation of regulated system operators which are already subject to corresponding, more specific requirements (e.g. under Article 37).
- **Limited definition of “indirect participant”** – Article 2(1), point (15)(a)(vii) extends the scope of eligible participants to “any other entity”. If a non-institution can be a participant, it should even more so be eligible as an indirect participant. Article 7(3), second subparagraph, in connection with the definition of the term “client” in Article 2(1), point (18), now acknowledges that transfer orders may also be entered into the system by clients. That clarification is highly welcome, in particular with regard to CCPs operating an Open Offer Clearing Model (where most market participants are not system participants, but where their orders – under the rules of the system – result in transactions and thus obligations of a system participant, e.g. under the principal-to-

⁶ ‘system’ means formal arrangement, other than an interoperability arrangement, with common rules and standardised procedures, including, a securities settlement system, a clearing system or a payment system, which provide for the settlement, clearing or execution of transfer orders between participants;

⁷ ‘Participant’ means any of the following entities, which participates in a system:

- (a) for designated systems, any of the following: an institution; a CSD; a settlement agent; a clearing house; a system operator, (vi) a clearing member of a CCP authorised pursuant to Article 17 of Regulation (EU) No 648/2012; a system member;
- (b) for registered systems, any member allowed under the rules of that registered system;

principal or other clearing models). We would propose aligning the third-country definition of “*participant*” with the EU definition, covering system operators, regulated entities, approved “*other*” entities, and approved indirect participants.

EACH proposal #6 – Explicit recognition of indirect participants

- EACH strongly suggests **explicitly including indirect participants** under the SFR protection (Art. 1(3)), to:
 - Reduce onboarding complexity;
 - Address legal uncertainty and Member State discretion.
 - Apply equally to third country systems.

EACH proposal #7 – Definition of “*indirect participant*” to be broadened to also cover entities listed in Article 2(1), point (15)(a)(vii)

- Against that above background, there appears to be no reason why the term “*indirect participant*” should be handled in a restrictive manner. The element delimitating “*indirect participant*” from “*client*” would appear to be that the indirect participant qualifies as a participant (Article 7(1)) and might therefore incur own obligations under the system rules (not limiting the responsibility of the participant through which the indirect participant passes transfer orders to the designated system).
- **EACH Members therefore suggest expanding the definition of “*indirect participant*” to be broadened to also cover entities listed in Article 2(1), point (15)(a)(vii).** That would accommodate a wider range of clearing models besides the Principal-to-Principal clearing model, i.e. established clearing models where the CCP enters into a direct contractual relationship with known clients (mostly non-institutions) of a clearing member, with the clearing member being ultimately responsible for the discharge of any obligations (e.g. as a guarantor). That is particularly true in relation to the clearing in the energy market, where financial players (clearing members) and non-financial players (trading participants and clients within the meaning of EMIR) are active.
- **Third-country CCPs should also be able to admit settlement banks, indirect participants and other kinds of participants.** The draft “*participant*” definition in a third-country context includes only a narrow category of “*members*”, a term whose interpretation depends upon how a system defines it but excludes numerous important actors in CCP systems. Participants such as system operators, settlement banks, delivery facilities, interoperating market infrastructure and indirect participants risk being excluded from scope. This situation departs from the SFD position, including under most member states' implementation of recital 7, under which system operators and other classes of participants (such as banks in the payment systems of CCPs and CSDs) are themselves also protected as participants. The insolvency of such entities could also have systemic impacts, were SFR protections not to apply.
- **Inconsistencies between the participant definition and concept of indirect participants should be addressed, and indirect participation should clearly be available to third-country systems.** While SFR Article 7(1) addresses indirect participants, the definition of “*participant*” does not, in either case, creating ambiguity. This is especially the case for third country systems, as it is unclear whether Article 7(1) applies to third country systems. By its text, Article 7 would appear capable of doing

so, but its linear position in the SFR would imply otherwise. The SFR should make clear provision in this regard. With increasing regulatory fragmentation, including as a result of various EU legislative initiatives, chains of participants are increasingly commonplace, especially among affiliates and especially for purposes of non-EU infrastructure connecting with EU users. It can be challenging for EU indirect participants to claim bankruptcy remoteness when offering services to their clients, in the absence of statutory insolvency law carve-outs for third-country systems, such as those applicable via the SFD/SFR. The possibility of indirect participation for third-country systems may therefore be important for EU financial institutions and their customers (as well as systems themselves).

EACH proposal #8 – Deletion of requirement on system operators to monitor compliance by system members with participation requirements

- The requirement on system operators to monitor compliance by system members with participation requirements (SFR Article 7) would lead to a double regulation of regulated system operators which are already subject to corresponding, more specific requirements (e.g. under EMIR Article 37). **This requirement should be deleted.**

Issue #5 – Default management and transfer orders

Article 1(2)

This Regulation also lays down requirements for the registration of third-country systems in one or several Member States in order to enable institutions established in those Member States, which participate in those third-country systems, to benefit from the extension of the insolvency protection provided for in Articles 17, 19, 22(1), 23, 24 and 25(1)⁸ to transfer orders entered into in such third-country systems.

In the case of an insolvency of a member of such a system, transfer orders entered by that member shall be protected where both the following conditions are met:

- a) the member participates in a registered system as defined in Article 2(1), point (9);*
- b) the member is an institution as defined in Article 2(1), point (10)(a)(i) to (iv) and (b), established in the Member State which has registered that system under Article 12.*

Article 17

1. Transfer orders and netting, including close-out netting, shall be legally enforceable and binding on third parties, provided that transfer orders were entered into the designated system or registered system before the moment of opening of insolvency proceedings as referred to in Article 22(1), even in the event of insolvency proceedings against any of the following: []

Transfer orders that are entered into a designated system or registered system after the moment of opening of insolvency proceedings and that are carried out within the business day, as laid down in the common rules and standardised procedures of such system, during which the opening of such proceedings occur, shall be legally enforceable and binding on third parties only where the system operator can prove that, at the time that such transfer orders become irrevocable, it was neither aware, nor should have been aware, of the opening of such proceedings.

⁸ Art. 17: Netting and transfer order; Art. 18: Moment of entry of a transfer order into a designated system; Art. 20: The moment of irrevocability of transfer orders; Art. 21: Final settlement; Art. 22: The moment of opening of insolvency; Art. 24: Law governing the rights and obligations of participants; Art. 25: Collateral security

2. No law, regulation, rule or practice on the setting aside of contracts and transactions concluded before the moment of opening of insolvency proceedings, as provided for in Article 22(1), shall lead to the unwinding of netting, or the disapplication of close-out netting provisions as referred to in Article 2(1), point (n), of Directive 2002/47/EC of the European Parliament and of the Council.

Article 19

The opening of insolvency proceedings against a participant or a system operator of an interoperable system shall not prevent funds or financial instruments available on the settlement account or on accounts holding collateral, including default fund contributions such as contributions to a pre-funded default fund held by a CCP in accordance with Article 42 of Regulation No 648/2012 and margins as referred to in Article 41 of Regulation No 648/2012, where applicable, of that participant or system operator from being used to fulfil that participant's obligations in the designated system, or registered system in the Member State where the participant is established, or in an interoperability arrangement on the business day of the opening of the insolvency proceedings.

2. Such a participant's credit facility connected to the designated system or registered system, as applicable, shall be usable against available, existing collateral security to fulfil that participant's obligations in the designated system, or in the registered system in the Member State where the participant is established, or in an interoperability arrangement.

Background

- **Protection of all relevant aspects of default management** – Considering that the SFR does not protect individual participants, but the financial stability of the system as a whole, it is necessary to stress that all aspects of the default management process, in particular those involving ownership of the defaulting clearing member before or after insolvency, including default actions (including transfer, close-out netting, collateral enforcement, hedging or contract management) and the application of the CCP default waterfall, should be included in any SFR protection.
- **Definition of transfer order** – The definition of “transfer order” under point (i) of SFD Article 2 contained two distinct alternatives:
“any instruction by a participant to place at the disposal of a recipient an amount of money by means of a book entry on the accounts of a credit institution, a central bank, a central counterparty or a settlement agent, or any instruction which results in the assumption or discharge of a payment obligation as defined by the rules of the system.”
This definition has been changed in SFR Article 2(1), point (20)(b).
- **Determination of irrevocability of transfer orders** – The additional criteria of entry, registration, and confirmation by the system (Article 18 (1) and 20 (1), respectively) may seem appropriate for many areas of application, but not for all. This applies in particular to the Open Offer Clearing Model, in which the CCP steps in between the buyer and seller upon the matching of orders by the relevant market, and where irrevocability is linked to the point in time that the orders are matched on the market.

EACH proposal #9 – SFR should explicitly protect all relevant aspects of default management and all cleared products as well as BAU activities

- The protection framework established by the SFR in cases of insolvency should be explicitly extended to **cover all relevant aspects of default management** carried out by the CCP — **before, during, and after a participant's insolvency**, in addition to

covering **business-as-usual activities (BAU)**. This is important because the SFR protections apply only to a relatively narrow part of CCP activities – dealing with transfer orders and security collateral – and exclude default management activities such as hedging on the clearing member’s account, rolling contracts, porting, auctions, realizing or transferring collateral and contracts, entering into of non-securities contracts (e.g. derivatives), managing open derivatives contracts or their risk management, the taking or netting of collateral received by way of title transfer (where the SFD could be interpreted as ambiguous and different Member State interpretations exist). Moreover, it is imperative to clarify the precedence of these specific rules over national insolvency laws, in line with the provisions of EMIR Article 48. This would provide CCPs with the solid, robust, and enforceable legal framework necessary to perform their core function of managing participant defaults when triggered by insolvency events.

- **Furthermore, protection should be extended to activities in relation to any assets (not just cash and securities)**. At present, protection is only granted for transfer orders entered on the day of insolvency, if “carried out” on that day, not after. If a transfer order is processed on the next day, it may therefore not be protected. This constitutes a problem for default management (if not otherwise protected) and also for settlement cycles longer than T+0. The full process of CCP default management typically takes 2-3 days from convening the default management group to auctions. We would suggest **clarifying the drafting of Article 19**, to ensure that the **full process of CCP default management is included** and avoiding any legal uncertainty.
- Although certain protections may arise for open derivatives under SFD, there is currently a major lacuna as regards deliveries under CCP-cleared derivatives in the SFD, which is not remedied via the SFR. The SFD only covers deliveries of securities upon expiry of e.g. cleared equity derivatives, as well as cash legs for all contracts and cash legs for cash-settled products. **Both SFD and SFR do not protect the finality of deliveries of commodities via CCPs under commodity derivatives. This should be reconsidered.** There is no reason, in our opinion, why a participant or indirect participant taking delivery of wheat, electricity, gas, sugar, voluntary carbon allowances, coffee etc via a CCP (and the CCP itself) should not be equally immune to insolvency law challenges as when taking delivery of products in the current scope (which are basically limited to cash, shares, emission allowances and bonds deliveries). The definition of transfer order should be expanded to cover all deliveries of all instruments via CCPs where the products are in-scope of their EMIR authorisation.
- We would also appreciate greater clarity on how the **conditions of registration under Article 14 should be assessed**, given that some of them are quite high-level (e.g. *“the system is governed by a law that upholds the principles of settlement finality”*) and that failure to meet any one of these conditions would result in registration not being granted.

EACH proposal #10 – Definition of transfer order to be reversed to the original one

- By deleting *“or any instruction”*, the new definition in SFR merges both alternatives into one, further tailoring the definition towards payment systems. The wording of the SFD could accommodate an even wider range of instructions, as long as they result in a payment obligation. That change should be reversed. Furthermore, there could be an

explicit recognition that CCPs clear transactions and that the payment and delivery obligations result directly from these transactions.

- We therefore suggest **reversing the definition of transfer order to the original one**.

EACH proposal #11 – Determination of irrevocability of transfer orders to be left to the rules of the system

- The determination of the point in time for the irrevocability of transfer orders **should be left entirely to the rules of the system** to avoid any potential conflict with, or ambiguity in relation to, established market practice.

Issue #6 – Collateral protection and digital/tokenised assets

Article 2(1), point (27)

'Collateral' means all realisable assets, including, without limitation, those financial instruments and funds, including those issued or recorded using distributed ledger technology, including in tokenised form, and financial collateral referred to in Article 1(4), point (a), of Directive 2002/47/EC, provided under a pledge, a title transfer arrangement, a repurchase or similar agreement, or otherwise, for the purpose of securing rights and obligations potentially arising in connection with or related to a system, or provided to central banks of the Member States or to the European Central Bank.

Background

- **Extension of the definition of collateral** – Article 2(1), point (27), expands the definition of to include DLT/tokenised assets.
- **Collateral definition must include margin and default fund received by CCPs** – We welcome the new express reference to the margin and default funds of CCPs within the SFR, as being a protected class of margin under Article 19(1). Issues as to the scope of collateral definitions are highly problematic in practice under the SFD, as has been identified by the Financial Markets Law Committee in a detailed paper dated November 2024⁹. The wording in Article 19 should be followed through to the other relevant provisions concerning margin, especially in the definition of *"collateral"*. There is also a current legal uncertainty as to the extent to which SFD provisions relating to collateral capture all margin and default fund held by CCPs. From a policy perspective, this would seem intended, but the related definition of *"transfer order"* only covers a part of the activity of CCPs; and default fund is an unusual sort of collateral (since it covers third party losses, not just those of the collateral taker). Currently, given that proposed SFR Article 25 does not include the same level of detail as Article 19, and because the scoping and definitional clauses in Articles 1(2) and 2(1)(27) of the SFR do not expressly pick up margin and default funds at CCPs, the wording appear inconsistent.

EACH proposal #12 – Support the extension of the definition of collateral

- In order to foster European CCPs' competitiveness as global level, EACH Members are in favour of the expansion of the definition of collateral suggesting including **DLT/tokenised assets**.

⁹ <https://fmlc.org/wp-content/uploads/2024/11/FMLC-Paper-Treatment-of-Collateral-under-SFRs.pdf>

- Also, **amendments should be made to the definition of collateral as well as the scoping wording in Articles 1(2) and 2(1)(27)**, as it would be important to clarify the scope of collateral as including both CCP margin and default fund, across the entirety of the SFR, rather than applying this only in limited situations
- Furthermore, **bank guarantees as defined in EMIR 3 Article 46 (also called letters of credit)** should be regarded as covered by the definition of collateral insofar as they qualify as realisable assets. While they are not currently considered as financial collateral under Directive 2002/47/EC (FCD)¹⁰, they can be enforceable and realisable in practice, and therefore fall within the broad, technology-neutral scope of SFR Article 2(1) point (27). Explicitly acknowledging this alignment would enhance legal certainty without expanding the framework beyond what is already coherent with the FCD (see also our comment below).

Issue #7 – The scope of the protection and realisable assets

Article 25(1)

The rights of a system operator or of a participant to collateral security provided to them in connection with a designated system, a registered system for its participants established in the Member States where the system is registered, or an interoperability arrangement, and the rights of central banks of the Member States or the European Central Bank to collateral security provided to them, shall not be affected by insolvency proceedings against any of the following:

- a) the participant in the designated or the registered system concerned or in an interoperability arrangement;*
- b) the system operator of an interoperable system which is not a participant;*
- c) a counterparty to the central bank of a Member State;*
- d) a counterparty to the European Central Bank;*
- e) any third party which provided the collateral security.*

Such collateral security may be realised for the satisfaction of those rights.

The rights of a system operator to the collateral security it provided to another system operator in connection with an interoperability arrangement shall not be affected by insolvency proceedings against the receiving system operator.

Background

- **Realisable assets** – Article 25(1) protects collateral security used in financial systems (like payment or settlement systems) from being affected by insolvency proceedings.

EACH proposal #13 – Explicit inclusion of realisable assets

- EACH Members suggest that the scope of the protections of Article 25 is clarified so that it **expressly includes also realisable assets** provided on a title transfer basis.
- Furthermore, to ensure full legal coherence, Article 25 should **expressly cover title-transfer collateral**. The FCD already recognises such arrangements as insolvency-resilient, and aligning the SFR with this framework would remove ambiguity and maintain consistency across EU collateral rules.

¹⁰ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32002L0047>

Issue #8 – Close-out netting

Article 17

1. *Transfer orders and netting, including close-out netting, shall be legally enforceable and binding on third parties, provided that transfer orders were entered into the designated system or registered system before the moment of opening of insolvency proceedings as referred to in Article 22(1), even in the event of insolvency proceedings against any of the following: []*

Transfer orders that are entered into a designated system or registered system after the moment of opening of insolvency proceedings and that are carried out within the business day, as laid down in the common rules and standardised procedures of such system, during which the opening of such proceedings occur, shall be legally enforceable and binding on third parties only where the system operator can prove that, at the time that such transfer orders become irrevocable, it was neither aware, nor should have been aware, of the opening of such proceedings.

2. *No law, regulation, rule or practice on the setting aside of contracts and transactions concluded before the moment of opening of insolvency proceedings, as provided for in Article 22(1), shall lead to the unwinding of netting, or the disapplication of close-out netting provisions as referred to in Article 2(1), point (n), of Directive 2002/47/EC of the European Parliament and of the Council.*

Background

- **Transfer orders and close-out netting protections** – The provisions in Article 17 clarify that transfer orders and netting, including close-out netting, are to be legally enforceable and binding on third parties, provided that transfer orders were entered into the system *before* the moment of opening of insolvency proceedings.

EACH proposal #14 – Close-out netting protections in resolution scenarios

- EACH Members suggest amending Article 17 so that **close-out netting protections apply not only in insolvency**, but also in **clearing member resolution scenarios where the CCP is subject to resolution measures**.
- It should also be clarified that the **inclusion of *other* claims and obligations** (e.g. claims and obligations of clients of participants) **in the netting** under the system rules does not negate the protection under SFR. This clarification would be helpful to accommodate established clearing models (in particularly clearing models other than the Principal-to-Principal Clearing Model), where the CCP enters into a direct contractual relationship with the client of a clearing member and where payment runs through the clearing member. This would promote efficiency of the post-trade process while ensuring legal certainty.

Issue #9 – Concepts of “possession” and “control”

Background & EACH Proposal #15 – Concepts of “possession” and “control” for security financial collateral to be clarified and harmonised

- For what concerns the concepts of “*possession*” and “*control*”, the lack of certainty as to how these apply to numerous commonly used collateral systems, e.g. where the collateral provider is able to withdraw collateral or where collateral remains in an account of the collateral provider. In the U.S., only post-default possession control is assessed, not the ongoing situation of possession or control and whether the level of

possession or control suffices, as in the EU. As a result, security financial collateral is essentially close to unused in Europe. Several Financial Markets Law Committee papers detail these issues, including with respect to the FCD. **The unclear definition of possession and control needs addressing as a high priority** and could, for example, be addressed via detail in technical standards. Such terms are not defined further in the FCD and, in most EU jurisdictions, are not legal concepts that could be readily used in relation to assets such as financial collateral. Further clarification could potentially be welcome, to the extent that it helps to provide more detail and harmonise the meaning of “possession” and “control” across Member States and so remove some of the uncertainty faced by market participants.

Issue #10 – Extension of SFR scope to (potentially unregulated) system operators

Article 5

A designating authority shall designate a system in accordance with Article 3, only where the designating authority is satisfied that all of the following conditions are fulfilled:

- (a) the system is governed by the law of the Member State of the designating authority;*
 - (b) at least one of the participants to the system is established in the Member State of the designating authority;*
 - (c) the system has common rules and standardised procedures for the settlement, clearing, or execution, as applicable, of transfer orders between the participants;*
 - (d) the system has clearly identified in its common rules and standardised procedures the moments of finality that fulfil the requirements set out in Articles 18, 20 and 21;*
 - (e) the common rules and standardised procedures of the system stipulate, where relevant in accordance with Article 7, the requirements for participation in the system;*
 - (f) there are no apparent conflicts between the common rules and standardised procedures of the system and the law governing the system;*
 - (g) the system operator is able to ensure adequate monitoring of compliance of its system with the common rules and standardised procedures of the system it operates;*
 - (h) the system operator is capable of operating the system, is of sufficiently good repute and has sufficient experience to ensure the sound and prudent management of the system;*
 - (i) the system operator has enough financial resources to operate the system;*
 - (j) the system operator is legally accountable, responsible and liable for the operation of the system, including for any links to other systems and the relationship to third parties and to the authorities;*
 - (k) the system operator has put in place sufficient measures to mitigate the risks related to the operation of the system;*
- [...]*

Background

- **Conditions for designating a system** – Within the newly proposed approval process, only those requirements that are relevant to the proper functioning of the protection mechanisms granted by the SFR should be examined (e.g. system rules that clearly define the moments of finality). The approval process should not extend to other supervisory requirements without such a direct connection (e.g., compliance, risk management, or financial resources). Otherwise, the SFR could result in double

regulation for system operators who are already subject to sector-specific regulations such as EMIR or Regulation (EU) No 909/2014 (CSDR)¹¹.

EACH proposal #16 – The approval process should not extend to other supervisory requirements without such a direct connection (e.g., compliance, risk management, or financial resources)

- In the context of the background above, we propose to **remove the requirements set out in Article 5(1)(g) to (k)**.
- If the scope of the SFR is extended to (potentially unregulated) system operators, the **above-mentioned requirements should not apply to regulated system operators such as CSDs and CCPs** (since these are already covered by sector-specific requirements under CSDR or EMIR).
- Specifically: the **requirement in Article 5(1)(b)**, which stipulates that at least one participant in the system must be established in the Member State of the designating authority, **may lead to a conflict of jurisdiction between the designating authorities in certain situations**, especially when the law governing the system does not coincide with the location of the system operator's registered office, and **should therefore be deleted**. In our view, the better approach would be to define the designating authority as the competent authority of the Member State in which the system operator is established.

Issue #11 – Risk of double regulation of regulated system operators

Article 7

2. A system operator of a designated system may accept a system member to the system only where that member meets all of the following conditions:

- (a) it has the capacity and ability to meet the obligations arising from its participation in the system;
- (b) it has the capacity and ability to mitigate the risks resulting from its participation in the system;
- (c) it complies with the rules of the system.

A system operator of a designated system shall establish admission criteria, differentiating per type of participant where relevant. Such admission criteria shall be non-discriminatory, transparent and objective to ensure fair and open access to the designated system.

A system operator of a designated system shall ensure that the system members comply with the conditions set out in the first subparagraph on an ongoing basis and shall have timely access to the information relevant for such assessment.

3. [...]

A participant that enables its clients to access the services of the system shall, upon request from the system operator, inform the system operator about the criteria and arrangements it adopts to enable its clients to access those services. Regardless of such information, that participant shall remain solely responsible with respect to the system operator and other participants to the system for ensuring that its clients comply with their obligations.

¹¹ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0909>

Background

- **Compliance monitoring** – The proposed SFR provision establishes that a system operator of a designated system shall ensure that the system members comply with the conditions set out in Article 7(2).

EACH proposal #17 – Deleting provisions forcing system operators to monitor compliance

- The **requirement on system operators to monitor compliance by system members** with participation requirements would lead to a double regulation of regulated system operators which are already subject to corresponding, more specific requirements (e.g. under EMIR Article 37 EMIR or CSDR Article 33). We therefore **suggest deleting such provisions**.

Issue #12 – Risk of conflicts with existing system rules regarding the moment of receipt of transfer orders in a designated system

Article 21

3. ESMA may, in close cooperation with the ESCB, for clearing and securities settlement systems not operated by a CSD, and taking into account the specificities of different types of systems, and the mechanics of those systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]

4. EBA may, in close cooperation with the ESCB, and taking into account the specificities of different types of payments systems and the mechanics of the systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]

EACH proposal #18 – Further amendments suggested

- Articles 21(3) and (4) provide **regulatory powers for ESMA and EBA** to determine, among other things, the moment of receipt of transfer orders in a designated system, the moment of irrevocability of a transfer order, and the moment of final settlement.
- Since these moments of finality are established by the rules of the system (see Title IV of the SFR), such regulatory powers could create conflicts with existing system rules or may not be compatible with the entirety of rules across different systems, leading to legal uncertainties. This is especially true for systems operated by regulated system operators.

EACH proposal #19 – Further amendments suggested

- We therefore propose the following amendments:
 - Article 21(3):
 - *“ESMA may, in close cooperation with the ESCB, for clearing and securities settlement systems not operated by a CSD **or a CCP**, and taking into account the specificities of different types of systems, and the mechanics of those systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]”*
 - Article 21(4):

- *EBA may, in close cooperation with the ESCB, **for payment systems not operated by a CSD or a CCP**, and taking into account the specificities of different types of payments systems and the mechanics of the systems, develop draft regulatory technical standards to specify the rules for determining all of the following: [...]*