



Relieve cash liquidity pressure on market participants by extending eligible non-cash collateral

(12 September 2022)

Summary

- In the context of addressing the energy crisis at EU and national levels EFET / the Associations welcome(s) the opportunity offered by the various emergency intervention proposals to underline the need to support well-functioning energy futures markets.
- EFET / the Associations further express(es) their full support to the adopted schemes at national levels and proposed measures at EU level to enable market participants to find the collateral to meet margin calls in financial energy markets.
- We urge EU authorities to provide an exceptional framework allowing CCPs to receive as collateral:
 - (i) the posting of fully committed on demand bank guarantees (in the sense of non-fully backed, unconditional and irrevocable on demand bank guarantees) issued in the favour of energy market participants; and
 - (ii) emission allowances or other accredited instruments,in order to immediately relieve the cash liquidity pressure.
- High and volatile wholesale energy prices continue to create significant cash liquidity pressure for energy market participants due to their impact on margin requirements on exchanges.
- The current situation is deteriorating and constraining participation in trading on exchanges, hindering the functioning of EU energy markets.



Current developments across the energy industry

As indicated in previous papers¹, it has become clear that rising prices both on energy exchanges and over-the-counter (OTC) are significantly affecting the economy. Multiple national and EU wide initiatives are underway to tackle the threats to industry and private households.

The recent [communication from DG ENER](#) *Short-Term Energy Market Interventions and Long Term Improvements to the Electricity Market Design* recognizes that emergency liquidity support measures should provide “relief for commodity traders and energy companies which are currently confronted with high margin calls on their derivative portfolio as a result of significant market volatility.”

New developments on energy markets increase the urge to implement rapid additional solutions for cash liquidity relief.

- **Quickly reintroduce fully committed on demand bank guarantees as eligible collateral**

Generally, while Article 46 [of Regulation \(EU\) No 648/2012 on OTC derivatives, central counterparties and trade repositories](#) (EMIR) allows the use of bank guarantees as collateral, currently, these commercial bank guarantees have to be fully backed by collateral. Previously, market participants used to trade under an exemption from the EMIR requirement for commercial bank guarantees to be fully backed by collateral, which expired in March 2016. Several clearing houses² in Europe historically allowed market participants to use such bank guarantees as collateral, especially energy clearing houses, as clearing members in those markets have limited amounts of cash or other collateral assets compared to financial market participants.

The requirement to fully backed commercial bank guarantees translates in reality to an almost complete ban on the use of bank guarantees as collateral for market participants, since it has the same effect as posting cash directly.

We urge to reintroduce the use of fully committed on demand bank guarantees issued in the

¹ [Joint Association Paper](#), *Access to short-term liquidity or guarantees provided by public entities and extension of eligible collateral will maintain the functioning of EU energy markets in times of extreme wholesale price development*, circulated in April 2022

² This is particularly the case for the clearing houses in the following jurisdictions: Denmark, Finland, Hungary, Poland, Portugal, Spain, Sweden and Norway.



favour of energy market participants in order to cover margin requirements related to their clearing activities, by removing section 2.1, point h) in Annex 1 in RTS (EU) No 153/20134, to cover partially the margin requirements and relieve the pressure on cash liquidity. These guarantees should be authorised to be passed through from the energy market participants to the CCP via the Clearing Members.

- **Allowing EU ETS emission allowances as additional eligible collateral**

Generally, accepting emission allowances to be posted as collateral would allow market participants to make use of their allowances more productively and economically.

Without the explicit recognition of emission allowances as an eligible type of collateral (under Art. 46 of EMIR regulation), the market participants cannot efficiently use their positions in emission allowances as collateral for central clearing. Their integration as eligible collateral could have a substantial effect regarding their acceptance as collateral in the overall market, in particular by clearing members and clearing houses. We agree to apply an eventual appropriate haircut to the value of emission allowances to establish the eligible collateral value at European level.

We urge to introduce the use emission allowances as eligible collateral to cover the margin requirements and relieve the pressure on cash liquidity.

The proposal will enable energy companies to post to some extent, as defined by CCP according to their risk assessment, these assets as collateral and will therefore mitigate, even though only partially, the pressure of market volatility on cash liquidity risk, without jeopardizing the risk management of the centrally cleared market.



Annex

Benefits of using bank guarantees:

Highly liquid products

Bank guarantees create a non-accessorial, abstract obligation to the beneficiary, putting the beneficiary in a strong legal position (“pay first, sue later”). The guarantor remains liable even if the underlying obligation is extinguished, it must pay immediately and cannot object. The feature of bank guarantees as unconditional, irrevocable and on first demand, make them “highly liquid”. For these continuing guarantees the guarantor assumes liability for any past, present and future obligations owed by a debtor to a lender or creditor. Even where the amount owing has been completely paid, the guarantor can still be liable under that line of credit if there is a subsequent indebtedness.

Limited market risk

The market risk of bank guarantees is limited in terms of volatility. In times of market stress, clearing members might find it difficult to increase the bank guarantee limits. This is mitigated by concentration limits on posted collateral per clearing member, i.e. limited percentage of its total collateral issued by one issuer.

Limited credit risk

Bank guarantees are only issued for companies owning assets and securing them will pose small risk for the bank. Hence, bank guarantees are a tool to solve the situation for energy companies cash-starved despite having valuable assets (i.e., being “cash short”, despite being “asset long”).

Further, the credit risk is managed by only accepting guarantees issued by investment-grade rated banks with a certain minimum rating, external rating and evaluation using an internal score card. A deterioration of a bank guarantee issuer’s credit worthiness will have implications on the applied haircuts and/or eligibility of the bank guarantees issued by the relevant bank. The lower the credit rating, the higher the haircut.

Low correlation between financial and energy sector

We underline the fact that potential risks can be measured and controlled, and that they do not lead to the argument that bank guarantees must be fully backed. The clearing house is exposed only to a loss in case both the member and the issuing bank are defaulting simultaneously. The



correlation of defaults in the energy sector and the financial sector has been historically low. Nevertheless, issuers may be added to the credit watchlist for extra monitoring. If an issuer defaults, the member is required to immediately find another issuer or collateral.

Attenuating the risk concerns of NFCs using non-fully backed bank guarantees

The purpose of reintroducing non-fully backed commercial guarantees is to allow market participants to cover the initial margin requirements in combination with cash. To the contrary of financial institutions, wholesale energy market participants using commercial bank guarantees as collateral have their capital tied up and invested in the real economy in assets (such as power plants) and commodities. Power plants (including their maintenance and reinvestments), storage facilities and commodities required for fuelling the plants are costly and represent an important value that can be cashed in upon an event of default.

These elements underline that the use of commercial bank guarantees as collateral by wholesale energy market participants does not increase any particular risk to the energy markets. In addition, there is no interdependence between the utilities sector and the banking sector which can limit the amount of bank guarantees based on the individual credit assessment of their respective clients. A simultaneous crisis of both sectors is highly unlikely.

About EACH

The European Association of CCP Clearing Houses (EACH) represents the interests of Central Counterparties Clearing Houses (CCPs) in Europe since 1992. EACH currently has 18 members from 14 different European countries and is registered in the European Union Transparency Register with the number 36897011311-96. EACH works with public authorities and industry stakeholders in order to offer the consolidated opinion of our membership in regulatory discussions and consultations as well as help member CCPs to agree appropriate standards and guidelines for the industry.

About EFET

The European Federation of Energy Traders (EFET) promotes and facilitates European energy trading in open, transparent and liquid wholesale markets, unhindered by national borders or



other undue obstacles. We build trust in power and gas markets across Europe, so that they may underpin a sustainable and secure energy supply and enable the transition to a carbon neutral economy. EFET currently represents more than 100 energy trading companies, active in over 27 European countries.

About Eurelectric

Eurelectric is the federation of European electric industry. We speak for more than 3500 European utilities covering the entire industry from electricity generation and markets to distribution networks and customer issues.

About Eurogas

Eurogas represents the interests of the European gas industry. We represent the entire gas value chain, from the gas wholesale market through distribution to retail. We also represent companies supplying end-user equipment and technology solutions. Our membership is composed of over 65 companies and associations in 24 countries.

About Europex

Europex is a not-for-profit association of European energy exchanges with 30 members. It represents the interests of exchange-based wholesale electricity, gas and environmental markets, focuses on developments of the European regulatory framework for wholesale energy trading and provides a discussion platform at European level.