26/01/2021

D E C I S I O N

Nasdaq Clearing Aktiebolag
via the Chairman of the Board of Directors
105 78 Stockholm

FI Ref. 18-23053
FI Ref. 18-23054
FI Ref. 18-24342
Notification No. 1

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Warning and administrative fine

Finansinspektionen's decision (to be announced 27 January 2021 at 8:00 a.m.)

1. Finansinspektionen is issuing Nasdaq Clearing Aktiebolag (556383-9058) a warning.

(Chapter 25, section 1 of the Securities Market Act [2007:528])

2. Nasdaq Clearing Aktiebolag shall pay an administrative fine of SEK 300,000,000.

(Chapter 25, section 8 of the Securities Market Act)

To appeal the decision, see *Appendix 1*.

Summary

Nasdaq Clearing Aktiebolag (Nasdaq Clearing or the firm) is a clearing organisation that holds authorisation to act as a central counterparty in accordance with Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR). A central counterparty acts as an intermediary on the securities market, as a buyer for every seller and seller for every buyer in all contracts that it clears. Given the concentration of counterparty risks that arises among central counterparties, they are considered systemically important. Strict rules, primarily through EMIR, thus apply to these types of operations.

Following the declaration of default on 11 September 2018 for one of Nasdaq Clearing's clearing members, Finansinspektionen investigated Nasdaq Clearing's handling of the default situation and how the firm complied with the

organisational, business conduct, and prudential regulations set out in EMIR. After Nasdaq Clearing informed Finansinspektionen that the firm had discovered errors in its calculation of margins, Finansinspektionen also investigated whether the firm was deficient in its monitoring and follow-up of these calculations, and as a consequence issued insufficient margin calls.

Finansinspektionen's investigations show that Nasdaq Clearing has had serious deficiencies in its operations. The investigations have demonstrated that there were obvious and significant deficiencies in how Nasdaq Clearing designed its participant requirements and how the firm followed up and monitored whether the members are fulfilling these requirements on an ongoing basis. The investigations have also demonstrated that Nasdaq Clearing has been in violation of the investment prohibition in EMIR by investing its resources in derivative contracts too long after the default event. The firm has also been issuing insufficient margin calls due to the incorrect calculation of margins. Together with other deficiencies that are presented in this decision, these breaches have created unacceptable risks in Nasdaq Clearing's operations, which could have had a very serious impact on the financial system. This justifies a strict assessment.

Nasdaq Clearing has taken measures to rectify some of these deficiencies. When deciding on the sanction, Finansinspektionen therefore made the determination that, despite the serious nature of the breaches, there is no reason to assume anything other than that the breaches will not be repeated, and it would be sufficient to issue Nasdaq Clearing a warning combined with a significant administrative fine. To reflect the serious nature of the deficiencies, Finansinspektionen considered in particular when deciding the administrative fine that the firm is systemically important and part of a large group. The size of the fine is therefore set at SEK 300,000,000.

Contents

1 Background

1.1 Clearing organisation, group and operations as central counterparty

Nasdaq Clearing Aktiebolag (Nasdaq Clearing or the firm) is an authorised central counterparty in accordance with Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR) since 18 March 2014, and FI considers the firm to be a systemically important institution. According to Chapter 1, section 1a of the Securities Market Act (2007:528), the firm is subject to Finansinspektionen's supervision pursuant to Chapter 23, section 1, first and second paragraphs of the same act.

Nasdaq Clearing provides central counterparty clearing of financial instruments traded both on exchange and OTC, primarily financial derivatives and commodity derivatives. The firm conducts its operations in Stockholm, with a branch in Oslo and a branch in Vilnius. On 31 December 2020, the firm had approximately 190 clearing members between its commodity market and financial markets. These members currently consist of only financial and non-financial companies (for example municipalities and municipally owned companies).

Nasdaq Clearing's most recently adopted annual report refers to the 2019 financial year. The annual report states that the firm had a turnover of SEK 563 million for the year and 67 employees.

Nasdaq Clearing is part of the Nasdaq Group, an international group with operations in, for example, the USA and the Nordic and Baltic countries. In 2019, the Group had a turnover of USD 4,262 million.

1.2 The investigations

Finansinspektionen discusses in this decision three investigations that it conducted into Nasdaq Clearing's operations as a central counterparty.

1.2.1 Compliance with EMIR, including default procedures and participant requirements

In September 2018, the spread between Nordic and German electricity prices increased sharply. This increase caused the only member of Nasdaq Clearing's commodity market that was a natural person to become illiquid since the member had pledged insufficient margins for its commitments and was not able to pledge the additional margin required due to the price fluctuations. On the morning of 11 September 2018, Nasdaq Clearing declared the member in default (hereafter "the default event"). Nasdaq Clearing then withdrew money from the so-called default fund to cover the losses that were incurred.

As a result of this default event, Finansinspektionen opened three investigations into how Nasdaq Clearing acted in conjunction with the default event (the default procedures), of which two are discussed in this decision (FI Ref. 18-23053 and 18-23054). The objective of the two investigations was to review the firm's compliance with the rules on investments, default procedures and participant requirements that apply to a central counterparty. Finansinspektionen intends to close the third investigation (FI Ref. 18-22977) without any further measures.

1.2.2 Configuration errors regarding the calculation of margins

Finansinspektionen also opened a fourth investigation after Nasdaq Clearing informed the authority in November 2018 that the firm had discovered a configuration error in its calculation of margins (FI Ref. 18-24342). The objective of Finansinspektionen's investigation into this part was to review how the firm monitors and follows up on its calculations and whether the firm issued insufficient margin calls.

1.2.3 Details on the administration of the investigation

As part of the investigations, Nasdaq Clearing has answered questions from Finansinspektionen. Finansinspektionen also held meetings with the firm.

During the spring of 2019, Finansinspektionen sent a verification letter to the firm for each of the investigations. The firm has answered these verification letters.

On 11 February 2020, Finansinspektionen sent a request for opinion to the firm. The request referred to all four investigations. Nasdaq Clearing thus had the opportunity to comment on the authority's observations and preliminary assessments while at the same time receiving the information that Finansinspektionen was considering intervention against the firm. The firm answered on 10 March 2020. On the same day, Nasdaq Clearing also submitted a document addressed to Finansinspektionen's Board of Directors.

Finansinspektionen sent a supplementary request for opinion to the firm on 30 September 2020. This request referred to the investigation into the handling of the default event (FI Ref. 18-23054) and related to how the firm had handled the so-called investment prohibition. The firm answered Finansinspektionen on 14 October 2020.

1.3 Structure of the decision

In addition to this background section, the decision contains five main sections.

Section 2 presents a brief overview of the provisions Finansinspektionen applies in the decision. The applicable provisions themselves are presented in more detail in Appendix 2.

In Section 3, Finansinspektionen presents a number of points of departure that make reading and understanding the decision easier. These positions are also of importance for Finansinspektionen's assessments in the following sections.

In Section 4, Finansinspektionen presents its observations and assessments in the investigations that are related to the default event (FI Refs. 18-23053 and 18-23054). Finansinspektionen states its position in this section on whether Nasdaq Clearing followed the rules on investments, default procedures and participant requirements that apply to a central counterparty.

In Section 5, Finansinspektionen presents its observations and assessments in the investigation related to the configuration error (FI Ref. 18-24342). Finansinspektionen states its position in this section on whether Nasdaq Clearing monitored and followed up on calculations of margins and issued insufficient margin calls.

In conclusion, in Section 6, Finansinspektionen presents its considerations regarding intervention against Nasdaq Clearing as a result of the observed violations.

2 Applicable provisions

This decision applies provisions from EMIR and Commission Delegated Regulation (EU) No. 153/2013[1] (hereafter "RTS 153") on the organisation, business conduct and prudential requirements that apply to a central counterparty. A more detailed description of these provisions is set out in *Appendix 2*.

Section 6 presents applicable provisions regarding intervention.

3 Points of departure

3.1 Terms and concepts

Some of the terms and concepts applied in this decision have different names in Swedish legislation than they do in EU legislation. However, their meaning is the same.

A firm that has received authorisation as a *central counterparty* is called a *clearing organisation* in Swedish legislation. The name in the Swedish legislation is mainly important in matters related to the classification of the firm according to Swedish regulations and when determining which provisions on

[1] Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on requirements for central counterparties, in its wording after 16 June 2016.

intervention are applicable. Both of the terms are used in this decision, and they refer to the firm Nasdaq Clearing and its operations.

Another difference is that EU legislation uses *clearing member* while Swedish legislation uses *clearing participant*. This difference is also not of significance. This decision uses almost exclusively the term from EU legislation.

In this context it can also be noted that EMIR contains the terms *participation requirements* and *admission criteria*, but there is no clear difference between the two. The decision uses the broader concept of *participation requirements* to describe the requirements that apply in general while using the term *admission criteria* primarily when referring to the criteria that a member must meet to gain admission to the clearing for the first time.

3.2 Central counterparties and their role on the financial market

EMIR was introduced in 2012 in the wake of the financial crisis. The regulation introduced new rules on mandatory clearing via a central counterparty for OTC derivatives declared appropriate for clearing. The requirement on mandatory clearing has changed derivatives trading. Large volumes of bilateral exposures that previously existed between individual parties were replaced by large exposures to central counterparties.

Under central counterparty clearing, the central counterparty acts as a buyer for every seller and seller for every buyer in all contracts that the central counterparty clears.[2] This moves the counterparty risk for each contract from the original parties to the central counterparty. This means that the risk management at systemically important central counterparties is crucial for the stability of the financial market.

A central counterparty thus functions as a type of intermediary or middleman on the derivatives market. Its function is to collect and thus reduce various risks on the market. The market risk for a central counterparty must be zero or close to zero since it is not an actor on the market but rather part of the market's infrastructure. This is why there are strict rules in EMIR and RTS 153 on how a central counterparty may invest its own resources, the so-called investment prohibition (see more below in section 3.4.2).

When the central counterparty steps in as both buyer and seller in a transaction, the risk elimination comes from a loss on one side of the transaction being fully compensated by a corresponding profit on the other side of the same transaction. In other words, there is always a counterposition to every position that the central counterparty clears. This requirement is usually referred to as the central counterparty having a *matched book* and is very important since this is how the

[2] In addition to the derivatives that are subject to the clearing obligation, large volumes of other derivatives not subject to a clearing obligation are also cleared.

central counterparty is protected from the market risk associated with the transactions.

3.3 Importance of the PFMI principles

The work to develop EMIR progressed in parallel with a global regulatory project within the International Organisation of Securities Commissions (IOSCO). In April 2012, shortly before EMIR was adopted, IOSCO and the Committee on Payment and Settlement Systems of the Bank for International Settlements (CPSS) published guiding principles for the infrastructure of the financial markets. These principles are called the *principles for financial market infrastructures (PFMI)*[3].

The PFMI are important for the application of several EU legal instruments in the area of finance, as presented in the recitals of each legislative act. The relationship between the PFMI and EMIR is evident from Recital 90 in EMIR, which states that EMIR follows the existing recommendations developed by CPSS and IOSCO. It also states that the European Securities and Markets Authority (ESMA) should consider the PFMI and future amendments to them when drawing up or proposing to revise the regulatory technical standards as well as the guidelines and recommendations foreseen in EMIR. Some of these principles are therefore mentioned expressly as underlying principles and as sources of interpretation in delegated regulations to EMIR, for example Recitals 2 and 46 of RTS 153, which Finansinspektionen applies in this decision.

In addition to making express references to the PFMI in EMIR and RTS 153, there are also guidelines issued by ESMA on the application of the PFMI.[4] The objective of these guidelines is to clarify that the intention of the legislator and ESMA for EMIR and related supervision and implementation regulations has been to consistently implement the PFMI. Finansinspektionen, like the competent authorities of the other EU Member States, is obligated to use all available means to try to follow these guidelines in its supervision.[5]

ESMA's guidelines state that when the competent authorities carry out their duties resulting from EMIR for the authorisation and supervision of central counterparties, they must ensure that the central counterparties within their territories comply with the requirements in EMIR in accordance with the PFMI. The authorities must also ensure that the central counterparties work in a manner that is line with the PFMI.

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[3] CPSS-IOSCO Principles for Financial Market Infrastructures, https://www.bis.org/cpmi/publ/d101a.pdf. In this decision, PFMI is used as an abbreviation for this document as well as for the principles themselves.

[4] Guidelines and Recommendations regarding the implementation of the CPSS-IOSCO Principles for Financial Market Infrastructures in respect of Central Counterparties (2014/1133).

[5] See Article 16(3), first paragraph of 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.

Even if the PFMI are not formally binding, the above means that, in this decision, Finansinspektionen is applying its principles as support for the authority's interpretation of the individual provisions set out in EMIR and RTS 153. The principles mentioned in this decision are mainly those that refer to participation requirements, the default procedures, and a central counterparty's own investments. The principles are only published in English. Their primary content is provided in conjunction with the references made to them.

3.4 Requirements placed on the operations (safe and sound requirements)

3.4.1 General requirements

Because EMIR introduces an obligation for counterparties to clear through central counterparties, the legislator has made the assessment that it is essential to ensure that central counterparties are safe and sound and comply at all times with EMIR's stringent organisational, business conduct, and prudential requirements (Whereas point 49 of EMIR). These safe and sound requirements are crucial for how the operations are to be run.

Therefore, this section describes briefly some of the main categories of the requirements placed on a central counterparties and relevant in the three investigations. The provisions on organisation, business conduct and prudential requirements are each set out in their own chapter in EMIR (see the summary of applicable provisions in *Appendix 2*), and this section follows the same breakdown.

Various delegated and implementing regulations, for example RTS 153, clarify the requirements that are set out in EMIR in order to ensure their consistent application. RTS 153 contains rules on, for example, organisational governance, margins and the default fund.

Organisational requirements

Since central counterparties comprise an important part of the infrastructure on the securities market, a central counterparty must fulfil several soundness requirements linked to how the firm is organised; see Title IV, Chapter 1 of EMIR. The organisational requirements relate to, for example, risk management, well-documented policies and procedures and adequate IT systems. Experienced senior management of sufficiently good repute, an independent risk committee, good record-keeping and suitable shareholders are additional requirements. The requirements also include the handling of conflicts of interest, the capacity for business continuity and rules on outsourcing.

Conduct of business rules

In addition to the requirements on the design of the organisation, EMIR contains rules on how a firm operating a central counterparty must act, so-called conduct

of business rules; see Title IV, Chapter 2 of EMIR. These rules are important since the operations must be run safely and soundly.

The conduct of business rules contain requirements on fair and professional behaviour, participation requirements, and transparency requirements with regard to, for example, prices and risks.

Prudential requirements

The requirements on safe and sound risk management constitute an important part of a central counterparty's operations. These requirements are called prudential requirements in EMIR; see Title IV, Chapter 3. A central counterparty must have a sound risk management system to handle, for example, counterparty risks, credit risks, market risks, and liquidity risks. A central counterparty must also have adequate procedures and mechanisms to handle a clearing member's default.

A central counterparty, according to EMIR, must limit its credit exposure to clearing members by collecting margins from them and establishing a default fund. A central counterparty must also have at its disposal sufficient liquidity to perform its services.

EMIR sets out an investment prohibition, under which a central counterparty may only invest its financial resources in cash or highly liquid financial instruments with minimal market and credit risks. The specific financial instruments in question are regulated in RTS 153. RTS 153 also contains more detailed provisions on the scope of the investment prohibition.

Other prudential requirements in EMIR are the so-called default waterfall principle, which specifies the order in which various financial resources must be utilised if a clearing member defaults, the requirement that collateral must have minimal credit and market risks, and the requirement on detailed default procedures when a member defaults. The prudential requirements also include that a central counterparty must regularly review the models and parameters used in its risk control.

The implications of the investment prohibition and the definitions of margins and default and how they are regulated are described in more detail in the following section.

3.4.2 More details on certain fundamental provisions

Participation requirements (Article 37 of EMIR)

The central counterparty must ensure that the members meet the necessary requirements to fulfil their obligations under EMIR, for example pledging margins and contributing to the default fund. The central counterparty must

ensure this by making sure its members meet the requirement on sufficient financial resources and operational capacity, the so-called participation requirements. These provisions are of central importance for ensuring that a member will not expose the central counterparty to unacceptable risks.

Margin requirements (Article 41 of EMIR)

Margins are described in the Whereas points in EMIR as a central counterparty's primary line of defence (Whereas point 70 in EMIR). Every buyer and every seller in every transaction that is to be cleared must pledge margins to guarantee their obligations to the central counterparty, or in other words to the members. This covers and neutralises the significant counterparty risks that would otherwise have accumulated at the central counterparty.

In order to calculate the margin requirements for each clearing member, according to Article 41(2) of EMIR, the central counterparty must apply models and parameters that capture the risk characteristics of the products cleared and take into account the interval between margin collections, market liquidity and the possibility of changes over the duration of the transaction. According to the same article, the competent authority must validate the models and parameters that the central counterparty uses. More detailed provisions on these parameters are set out in Articles 24–26 of RTS 153.

Default fund (Article 42 of EMIR)

In addition to margins, central counterparties also collect contributions from each member to finance the *default fund*, which is to cover losses arising from the default of one or more clearing members and that exceed the losses to be covered by the margin requirements. A clearing member thus contributes to covering the losses from the default of other clearing members.

Prohibition on certain investments (Article 47 of EMIR)

According to Article 47(1) of EMIR, a central counterparty may only invest its financial resources in cash or other highly liquid financial instruments with minimal market and credit risks (see Whereas point 46 of RTS 153 with a reference to Principle 16 of PFMI). Annexes I and II of RTS 153 regulate in more detail the conditions applicable to these allowable investments. Investments other than those stated there are as a main rule prohibited (the investment prohibition). The investment prohibition applies in part to derivative contracts.

The investment prohibition is not absolute. With regard to derivative contracts, there are two specific exemptions from the main rule. According to one of these exemptions, a central counterparty may invest in derivative contracts to hedge the portfolio of a defaulted clearing member (point 2 of Annex II of RTS 153). A condition for applying this exemption is that the use of derivative contracts must

be limited to the period of time necessary to reduce the credit and market risk to which the central counterparty is exposed. The reason that derivative investments may only occur under these very limited conditions is that these types of investments expose the central counterparty to additional credit and market risks and that a central counterparty should always strive for a flat position with regard to such risks (Whereas point 47 of RTS 153).

Closing out of positions given default (Article 48 of EMIR)

A clearing member can default if it is not able to meet its financial obligations arising from being a member. A default event requires prompt action to protect the operations, the members and the risk management of the central counterparty. Article 48(2) of EMIR therefore states that a central counterparty, faced with the default of a member, must take prompt action to contain losses and liquidity pressures. According to the same article, a central counterparty must ensure that the closing out of any clearing member's positions does not disrupt the central counterparty's operations or expose the non-defaulting clearing members to losses that they cannot anticipate or control.

In order to handle the stress to the financial market arising from the handling of the default, the positions associated with the default event must be closed out quickly and carefully, for example through netting of transactions or transfer. The central counterparty thereby fully eliminates its risks associated with the positions affected by the default. Since the idea behind the central counterparty's operations is to concentrate counterparty risks to one entity, it is crucial for financial stability that the central counterparty not contribute itself to further imbalances on the market. As a main rule, therefore, the central counterparty is not allowed to take on any risk itself when the positions are being closed. The consequence could otherwise be that the central counterparty takes on unsustainable risks and defaults itself. In all probability, this would have a very large impact on the entire financial system.

The requirements outlined above on what a central counterparty must consider during a default situation is well in line with that set out in section 3.13.4 of PFMI, which states that there is a rising risk of potential risks due to price movements or changed market conditions in general the longer a central counterparty's own financial resources are exposed to market fluctuations within its handling of the default. The same section also emphasises that a central counterparty, within its handling of the default, should have sufficient information, resources and tools to close out its positions promptly. It also states that if a prompt close out is not possible, a central counterparty should have the necessary tools to hedge the positions as an interim risk-management technique.

4 Review of how Nasdaq Clearing complies with organisational, business conduct and prudential requirements

4.1 Participation requirements

A central counterparty, as described above, must establish participation requirements for clearing members to participate in the clearing activities. The provisions for such requirements are set out in Article 37 of EMIR and constitute a part of the conduct of business rules that apply to a central counterparty. The article states that a central counterparty must ensure that the clearing members have sufficient financial resources and operational capacity to meet the obligations arising from participation in a central counterparty. It also states that the participation requirements must be non-discriminatory, transparent and objective so as to ensure fair and open access to the central counterparty.

A firm operating a central counterparty, pursuant to Article 26(2) of EMIR, must also adopt policies and procedures which are sufficiently effective so as to ensure compliance with EMIR. This requirement constitutes a part of the organisational requirements that apply to a central counterparty.

Finansinspektionen has investigated how Nasdaq Clearing has complied with the obligations set out in Articles 37 and 26 of EMIR. As part of this investigation, Finansinspektionen has received, among other things, Nasdaq Clearing's policies and procedures on participation requirements.

4.1.1 Content of the participation requirements

The participation requirements, including the admission criteria, fulfil a central function in monitoring the counterparty risks in the clearing operations. Therefore, it is very important that a central counterparty both establish appropriate requirements and regularly ensure compliance with them.

Nasdaq Clearing's participation requirements for the commodities market and the financial markets at the time of the investigation were outlined in the firm's clearing rules and credit risk policy[6].

Both of these documents state (according to their wording in September 2018) that the potential member must be suitable for the member category in question and participation in the clearing activities. They also state the applicant must have sufficient financial resources, an appropriate organisation, sufficient competence, requisite risk-management procedures and appropriate and secure technical systems. In terms of financial resources, the documents state that a clearing member must also have financial resources at its disposal that at any given point in time corresponds to the activities the member intends to perform on the relevant market, although no less than a specified minimum amount.

In addition to that mentioned above, the documents state that Nasdaq Clearing, with regard to certain member categories, requires that the member be a certain type of legal entity with special authorisation from a competent authority. They also state that for all member categories Nasdaq Clearing may grant exemption

[6] Nasdaq Clearing AB Credit Risk Policy.

from the admission criteria if the member is still considered suitable for participating in the clearing activities.

There is no additional information in the clearing rules, credit risk policy or any other documents about the participation requirements, including the admission criteria, or a more detailed description of what the requirements entail.

4.1.2 Nasdaq Clearing's participation requirements do not ensure that the clearing members have sufficient financial resources

As set out in Article 37(1) of EMIR, a central counterparty must establish participation requirements and admission criteria to ensure that the clearing members have sufficient financial resources to meet their obligations arising from participation. According to Finansinspektionen, this means that the central counterparty's participation requirements must be designed to take into consideration the risks that each individual member pose to the central counterparty and other members. For example, this may mean the risk that the member cannot meet the margin requirements arising from the member's positions. This interpretation is in line with Principle 18 of PFMI. Sections 3.18.1 and 3.18.5 of PFMI state in part that a central counterparty should control the risks to which it is exposed from its participants by setting risk-related requirements for participation. They also state that the central counterparty must ensure that its members have the requisite financial resources to prevent unacceptable risk exposure for the central counterparty and other members.

In terms of its members' financial resources, Nasdaq Clearing requires that applicants must have at their disposal a minimum amount of capital. How large this amount is varies depending on which member category the presumptive member wants to join. The firm has three member categories for the commodities market and three member categories for the financial markets. The minimum capital requirement has been the same for all members in each member category.

Nasdaq Clearing also required that its members must have at their disposal financial resources that at any given point in time correspond to the activities the member intends to perform on the relevant markets. Based on the information provided by Nasdaq Clearing as part of the investigation, Finansinspektionen has understood that the firm with this wording intended for the members, on an ongoing basis, to be able to make payments, provide collateral, meet margin requirements, and contribute to the default fund within the specified period of time.

According to Nasdaq Clearing, the minimum capital requirement means that the presumptive member undertakes to maintain a certain level of capital depending on the type of structural activities it carries out. The firm has explained that the objective of minimum capital rules is primarily to ensure that the members have a certain degree of financial robustness; the objective is not for the requirements to be adapted to and take into account all of a member's planned activities.

Nasdaq Clearing takes the position that the capital requirements applied by the firm ensure that the members are sufficiently financially robust and thus capture the risks pursuant to Article 37(1) of EMIR.
Finansinspektionen notes that the firm's requirement on sufficient financial resources has been designed in such a manner that the requirement is not placed in relation to the exposures an individual member has had or is allowed to have. The capital requirement has instead been dependent on the member category to which the member belongs. The difference between these member categories primarily consisted of whether the member may clear for itself or also for some other parties. There has not been any limitation in terms of the size of exposures that a certain member category may have. Nasdaq Clearing's participation requirements regarding sufficient financial resources, thus, in practice, have only consisted of the category-based minimum capital requirement.

Through its participation requirements, including the admission criteria, a central counterparty must ensure that the clearing members have sufficient financial resources to meet their obligations arising from participation. According to Finansinspektionen, the capital a clearing member should have must be placed in relation to the risk the individual member exposes the central counterparty and other members to through its exposures. In other words, it must be set individually; otherwise, the requirement would not fulfil any real function. The focus is not only on the risk that the member cannot meet its obligations as a clearing member, primarily by not being able to pay the margin call issued by the central counterparty based on the member's current exposures, but also ultimately on the risk of default. Therefore, general capital requirements that are not supplemented with other risk-mitigation methods that place the capital in relation to the risks the individual member is exposing the central counterparty to – for example, an exposure limit – do not meet the requirements laid down by the regulatory framework on how to assess whether the individual member's financial resources are sufficient.

Overall, Finansinspektionen finds that Nasdaq Clearing's requirement on sufficient capital at the time of the investigation only consisted of one minimum capital requirement per member category in a few categories and did not take into account the risk that the individual member posed to the firm. This means that Nasdaq Clearing did not establish participation requirements that ensure clearing members have sufficient financial resources to meet their obligations arising from the participation, which constitutes a breach of Article 37(1) of EMIR.

4.1.3 Nasdaq Clearing has not had policies and procedures that are sufficiently effective for ensuring that the participation requirements on operational capacity are met

According to Article 37(1) of EMIR, a central counterparty must also have participation requirements that ensure that each clearing member has sufficient operational capacity to meet their obligations arising from participation in a central counterparty. This also includes assessing the risks that an individual

member poses to the central counterparty and other members (cf. Principle 18 of PFMI). According to the same article, the participation requirements must be non-discriminatory, transparent and objective so as to ensure and open access to the central counterparty. Article 26(2) of EMIR states that a central counterparty must adopt policies and procedures which are sufficiently effective so as to ensure compliance with EMIR.
In terms of the operational capacity of its members, Nasdaq Clearing's clearing rules and credit risk policy state that the firm requires "suitable" organisation, "sufficient" level of competence, "necessary" risk management procedures, "suitable and secure" IT systems, and that the member also in general is considered "suitable" for participating in clearing activities.

Nasdaq Clearing has stated that its requirements on operational capacity are thus sufficiently concrete to fulfil the objective set out in EMIR. The firm takes the position that the requirements ensure that a member can make payments, provide collateral for positions taken, meet margin calls, and contribute fully to the default fund within the specified period of time. According to the firm, requirements on operational capacity are not quantifiable in the same way as financial requirements; they are by nature more general. The firm furthermore states that the requirements on the operational capacity of members are such that they are either met or not met, and that they therefore have always been sufficient.

The requirements on operational capacity that are set out in the above-mentioned documents are general in nature and do not contain more detailed explanations of what the requirements entail. The investigation shows that Nasdaq Clearing did not have any other policies or procedures that describe what the requirements of being "suitable", "sufficient" and "necessary" entail. The firm also did not have any policies or procedures describing how to carry out the assessment of the requirements on operational capacity or which specific circumstances the firm must consider during such an assessment.

Finansinspektionen notes that a certain degree of generalisation is unavoidable in policy documents and procedures. The wording used in the clearing rules and credit risk policy on participation requirements in terms of operational capacity, however, is so general that it more or less lacks content when, like in this case, there are no instructions to clarify the meaning. The absence thereof introduces a risk that the firm will not establish sufficient requirements for its members in terms of operational capacity. This also introduces a risk that the participation requirements are not being applied in a non-discriminatory and objective manner as required by EMIR (Article 37(1)).

Finansinspektionen therefore makes the assessment that Nasdaq Clearing has not followed the requirement set out in Article 26(2) of EMIR by not having policies and procedures that have been sufficiently effective to ensure that the participation requirements on operational capacity meet the requirements set out in EMIR.

4.1.4 Deficiencies in transparency with regard to the participation requirements

Article 37(1) of EMIR states that the participation requirements must be transparent. This means, for example, that it should be clear for the market and the public in general which specific admission requirements must be met to become a clearing member.

As presented in the previous section, Nasdaq Clearing's requirement on operational capacity has been vague and overly general. These rules, for the same reason, have not been transparent in the above-specified meaning. This is a deficiency and a breach with regard to Article 37(1) of EMIR.

In addition, Finansinspektionen states the following.

It is extremely unusual for natural persons to participate as clearing members in a central counterparty. This construction is justified. According to Finansinspektionen, there is normally a significantly higher risk associated with admitting a natural person as clearing member than admitting a legal person.

Until 30 September 2019, Nasdaq Clearing accepted private individuals as clearing members in a certain member category on the commodities market. It is not contested that this circumstance was only addressed indirectly by the clearing rules since they, for the member category in question , did not require a member to be a legal person. Nasdaq Clearing has asserted, however, that it has been known that the firm had a private individual as a member and pointed to information about its members on its website.

Finansinspektionen takes the position that it is particularly important for a central counterparty's admission criteria to clearly state whether natural persons may be admitted as members and, if they may, the requirements they must meet. It is not sufficient for this be addressed indirectly by the clearing rules or a list on the central counterparty's website. A central counterparty can also not assume that the market is aware of such a circumstance. Finansinspektionen therefore takes the position that in this respect Nasdaq Clearing also did not fulfil the requirement set out in Article 37(1) that the participation requirements must be transparent.

4.1.5 Deficiencies in ongoing control of the clearing members

Article 37(2) of EMIR states that a central counterparty must ensure on an ongoing basis that the clearing members comply with the participation requirements.

Finansinspektionen's investigation shows that Nasdaq Clearing's ongoing control consisted of continuous monitoring of not only each member's daily activities but also how each member meets their ongoing obligations to Nasdaq Clearing (such as the obligation to post margins).

Nasdaq Clearing is of the opinion that the day-to-day monitoring is the natural starting point of all compliance controls and that it is the best way to see if a member is having trouble meeting its obligations arising from the regulatory framework.

Finansinspektionen would like to emphasise that the participation requirements, including the admission criteria, are an important component of a central counterparty's risk management. The objective of these requirements is to manage the risks associated with participation and thus ensure that the clearing members have sufficient financial resources and operational capacity to meet their ongoing and other obligations arising from participation. Given that a member once was able to post the required collateral and contribute to the default fund does not necessarily mean that the member will also be able to meet the participation requirements continuously.

Finansinspektionen first notes that the day-to-day monitoring of the clearing members' actions as described by Nasdaq Clearing does not include any ongoing control of whether the members still meet the requirement on operational capacity. In other words, there have not been any ongoing controls of the members' operational capacity.

The investigation also shows that Nasdaq Clearing only ran a control once a year of the requirement that a member have sufficient financial resources. It did so as part of its annual review of whether the members meet the firm's minimum capital requirements. Finansinspektionen takes the position that this is not sufficient for meeting the requirements on ongoing control. Market conditions can change quickly, as the default event in 2018 shows. Given this background, it is necessary to perform controls on several occasions throughout the year.

Given the background described above, Finansinspektionen makes the assessment that Nasdaq Clearing has not met the requirement set out in Article 37(2) of EMIR to ensure on an ongoing basis that the participation requirements are met.

4.1.6 Deficiencies in the annual review of clearing members

In addition to performing ongoing controls, according to Article 37(2) of EMIR, a central counterparty must also conduct at least once a year a comprehensive review of compliance with the participation requirements by its clearing members.

Finansinspektionen's investigation shows that Nasdaq Clearing's annual review of its members consisted of a new credit risk assessment and controls that the member meets the minimum capital requirement for the member category in question and the member's shares have been listed during the year. The credit risk assessment was based on financial data from the members' most recent annual reports that was obtained from an external supplier as new annual reports are published. This information was then entered into Nasdaq Clearing's credit

assessment model to generate a new credit risk rating. If the result of the credit risk assessment demonstrated a negative change in the credit risk rating, the firm could decide to conduct a deeper analysis to determine whether the member must be added to its "credit watch list". The member, in such a case, would then be subject to more frequent monitoring. The control that the member meets the minimum capital requirement has also been based on the financial information from the member's annual report.

Since Q4 2018, Nasdaq Clearing has begun to request information through a so-called due diligence form that contains questions about members' financial resources and operational capacity and that members must answer every year. Before this form was introduced, the firm conducted no annual review at all of the members' operational capacity.

Nasdaq Clearing conceded in its opinion that it had insufficient procedures for the annual review of operational capacity before the new procedures were introduced in 2018 and that it thereby has not fully complied with the requirements set out in Article 37(2) of EMIR. In terms of the annual review of the members' financial resources, Nasdaq Clearing states that information from an adopted annual report must reasonably be considered reliable with the aim of conducting such an annual review. The firm emphasises, however, that there has been considerable room for improvement when it comes to this part of the annual review of its members.

As conceded by Nasdaq Clearing, it is a violation of EMIR that, during the investigation period, the annual review did not include the operational capacity. Finansinspektionen also notes that the firm's review of its members' financial resources has only been based on the information in each member's most recent annual report. Even if it can be assumed that the information in the annual report is correct at a given point in time, there is always a risk that it is no longer up to date at the time of the annual review. In order to conduct an acceptable review of the members' financial resources, the control must be based on up-to-date figures. Simply collecting information from the annual report, therefore, cannot be considered sufficient for meeting the requirements set out in EMIR:

Given that specified above, Finansinspektionen makes the assessment that Nasdaq Clearing did not meet the requirement set out in Article 37(2) of EMIR on conducting a comprehensive review of compliance with the participation requirements by its clearing members.

4.1.7 Finansinspektionen's conclusions regarding the participation requirements

Finansinspektionen's investigation identifies clear and significant deficiencies in how Nasdaq Clearing designed its participation requirements and how the firm followed up on and ensured that its members meet these requirements on an ongoing basis. In addition, the firm has not had policies and procedures in some areas that were sufficiently effective to ensure compliance with the provisions on participation requirements in EMIR. The deficiencies in question could have

serious consequences. The participation requirements are a very important tool for a central counterparty in terms of managing the counterparty risks arising in the operations.

Overall, Finansinspektionen takes the position that the observed breaches have meant there has been a concrete risk that Nasdaq Clearing has not placed sufficient requirements on its members in terms of either financial resources or operational capacity. Thus, the firm may have been exposed to higher counterparty risk than what is acceptable for a central counterparty, which the default event that actually occurred also clearly indicates. This is particularly serious since Nasdaq Clearing is a systemically important actor whose deficient risk management could ultimately have an impact on the stability of the financial markets.

4.2 Management of the default event

When a clearing member is declared in default, a central counterparty must follow special rules regarding the default procedures. These rules are set out, for example, in Article 48 of EMIR and constitute a part of the prudential requirements that apply to a central counterparty. The default procedures also include some exemptions from the investment prohibition set out in Article 47 of EMIR.

A firm operating a central counterparty also has an obligation under Article 36(1) of EMIR to act professionally in accordance with the best interests of the clearing members and their clients and in accordance with sound risk management. The provisions set out in the last-mentioned article constitute a part of the conduct of business rules that apply to a central counterparty.

In this part of the investigation, in addition to the information obtained from meetings and written questions, Finansinspektionen reviewed press releases that were published due to the default event.

4.2.1 Details of the event

On 11 September 2018, it became known that one of Nasdaq Clearing's members (the defaulting member) was in default. The defaulting member was the only clearing member who was a natural person. On the same day and the following day, Nasdaq Clearing held an auction procedure related to the positions affected by the default (the defaulted portfolio). The defaulting member's portfolio was not auctioned off; rather, what was auctioned was an offer to enter into certain contracts with Nasdaq Clearing. The contracts were placed in a newly created portfolio (the mirror portfolio) that mirrored the defaulting member's derivative holdings in the defaulted portfolio.

The mirror portfolio was created by Nasdaq Clearing, to the greatest extent possible, taking positions in derivatives that had the same underlying assets as in the defaulted portfolio but where the market risk went in the opposite direction (upturn was matched against downturn, profit against loss, etc.). As Finansinspektionen will return to, however, the creation of the mirror portfolio did not fully neutralise the risk since it was not possible to create a perfect mirror of the defaulted portfolio. The reason for this was that the derivative positions that Nasdaq Clearing took in the mirror portfolio did not always have the same underlying assets as those that were in the defaulted portfolio. The new derivative contracts also contained conditions for close out, for example, that deviated from the conditions of the contracts they were intended to reflect.

After the auction procedure, Nasdaq Clearing registered the contracts with both the auction winner's clearing account and the defaulting member's clearing account. As a result, a hedging transaction of the defaulted portfolio was created, which remained in the defaulting member's account. Nasdaq Clearing held this hedge until June 2019, when both it and the defaulted portfolio were transferred to a third party. Until the two portfolios were closed out (i.e., sold), it is Finansinspektionen's understanding that Nasdaq Clearing's own resources were exposed to market fluctuations in both the defaulted portfolio and the mirror portfolio and that the firm thus was responsible for any movements in price.

The default event incurred significant losses for Nasdaq Clearing's members. The members consisted of both financial and non-financial firms such as municipalities and municipally owned enterprises. The losses were incurred because the members needed to contribute to the replenishment of the default fund after part of it had been utilised. Nasdaq Clearing partly covered these losses by paying out around EUR 20 million to its members. The final losses for the members according to the firm were between SEK 250 and 350 million.

4.2.2 More details on the implications of the regulatory framework

The design of the regulatory framework is such that Article 48 of EMIR primarily governs the protection of the clearing members and the operations in the event of a default. According to this article, a central counterparty, given a default event, must act promptly and ensure that the central counterparty's operations can continue without disruptions. Another important aspect of the default management rules is to protect the clearing members from losses.

As described above in section 3.4.2, Article 47(1) of EMIR states that a central counterparty may only invest its financial resources in cash or highly liquid financial instruments with minimal market and credit risks. For other types of financial instruments or assets, an investment prohibition applies as a general rule of thumb. As mentioned above, however, point 2a of Annex II of RTS 153 allows for an exemption from the investment prohibition for derivative contracts that a central counterparty enters into with the objective of hedging a portfolio of a member in default (as part of the central counterparty's default procedures). The exemption applies on the condition that the use is limited to the period of

time necessary to reduce the credit and market risk to which the central counterparty is exposed. Whereas point 47 of RTS 153 also implies that the exemption must be interpreted restrictively, which according to Finansinspektionen means that the application of the requirement of a prompt close out of any derivative contracts that a central counterparty may have invested in must be applied stringently.

Other than the exemption from the investment prohibition in point 2a of Annex II to RTS 153, which refers to the application of Article 47 of EMIR on guidelines for investments, there are no provisions dealing expressly with the actual default management in the delegated regulation.

According to Finansinspektionen, it is clear that the exemption from the investment prohibition only aims to give a central counterparty the possibility of *temporarily* managing the risks in the positions immediately following the default incident. This conclusion is also fully in line with that set out by the PFMI, for example the reference to there being increasing risk due to price fluctuations or changed market conditions in general the longer a central counterparty's own resources are exposed to market fluctuations during the management of the default (see section 3.13.4 of PFMI). According to Finansinspektionen, this means that a central counterparty that wants to apply the exemption from the investment prohibition must assert circumstances showing that the investment has been limited to the period of time required to reduce the credit and market risk to which the central counterparty had been exposed.

4.2.3 Nasdaq Clearing's position

Nasdaq Clearing has denied that the firm breached the investment prohibition and primarily asserted the following.

The mirror contracts closed in full all remaining credit and market risk and thus created a perfect hedge for the defaulted portfolio. It is therefore not possible to say that a quick sale of the contracts would have been necessary to reduce the risk.

Even if it could be said that there still was a remaining credit and market risk, it is the position of Nasdaq Clearing that it was necessary for the firm to hold the mirror contracts as long as the corresponding contracts in the defaulted portfolio were held. If the firm would have sold the mirror contracts before the defaulting member's corresponding contracts had expired, the firm would have been once again exposed to the market risk in the defaulting member's contract. This could not have been the intent of the regulation.

Where the investment prohibition would be applicable, Nasdaq Clearing has asserted that the derivative contracts continued to be more attractive from a transfer perspective even after the start of the new year up to the point when they were transferred. According to the firm, it is also natural that the transfer occurred at the end of the quarter in order to provide enough time to prepare

operationally and carry out the move since contracts in delivery cannot be transferred. Nasdaq Clearing was also working with the transfer process during the spring of 2019 with the aim of transferring the contracts to a third party at as low a cost as possible. There was also no disadvantage or risk to keeping the contracts during this time since Nasdaq had kept sufficient margin requirements to cover the payment obligations that would arise as the contracts in the portfolio expired and since the portfolio was perfectly hedged.

4.2.4 Nasdaq Clearing disregarded the investment prohibition

Starting points for the assessment

Finansinspektionen notes that Nasdaq Clearing, when the default event occurred, initially reacted promptly and in accordance with the provisions set out in the regulatory framework. However, there was no actual sale of either the defaulting member's positions in the defaulted portfolio or the positions that Nasdaq Clearing took in the mirror portfolio until June 2019, in other words ten months after the default event.
It is not contested that Nasdaq Clearing, in conjunction with the default event, invested in derivative contracts when the firm created the mirror portfolio.

The way that Nasdaq Clearing chose to act meant that the firm's own resources were exposed to market fluctuations in the mirror portfolio, and in practice in the defaulted portfolio as well, until June 2019. Nasdaq Clearing's actions resulted in the firm being responsible for the risk for any price fluctuations in both portfolios.

It is clear that the investments in derivative contracts were initially made as part of Nasdaq Clearing's management of the default event. As stated, the regulatory framework allows investments in such contracts if they occur to hedge a portfolio of a defaulting member but then only for the period of time required to reduce the credit and market risk to which the central counterparty is exposed. The question that Finansinspektionen has to consider is whether the exemption from the investment prohibition was applicable during the entire period that Nasdaq Clearing held the exposure, in other words until June 2019.

Occurrence of credit and market risk

In this assessment, Finansinspektionen can first note that it does not share Nasdaq Clearing's view that the defaulted portfolio and the mirror portfolio together neutralised the risk.

This is because, first, Nasdaq Clearing, through the firm's choice of using two portfolios, did not have a so-called matched book. Losses on one side of a transaction have not been fully compensated for by corresponding profits on the other side of the same transaction. The reason for this is that the defaulted portfolio and the mirror portfolio – despite strong correlation – consisted of

contracts with different characteristics and conditions, for example with regard to close out. The market valuation of the contracts in the two portfolios, therefore, has been different.

Second, the cash flow did not match since the derivative contracts in the defaulting member's portfolio and the contracts in the mirror portfolio did not have identical conditions. The portfolios contained different types of derivative contracts, which meant that profits and losses in the defaulted portfolio were not realised at the same time as the corresponding losses and profits in the mirror portfolio. While waiting for the derivative contracts in the two portfolios to fall due and give rise to a corresponding income, Nasdaq Clearing has thus been responsible for, and even needed to replace, the deficiency with its own resources.

Third, it can be noted that Nasdaq Clearing in practice has not managed the defaulted portfolio as a flat position. The investigation shows that Nasdaq Clearing's margin model rendered a margin requirement for the remaining positions, even if it was a relatively limited requirement, when they were finally transferred to a third party in 2019.
Finansinspektionen therefore rejects Nasdaq Clearing's objection that it was a matter of a perfect hedge. It can also be noted that, in the investigation, Nasdaq Clearing has admitted that there were deficiencies in the cash flow matching and that there thus had been a risk but asserted that the firm had managed this risk through hedging transactions. The firm has also granted that it was not possible to hedge all imbalances in the cash flow matching but objected with the argument that the outstanding deficiency would be covered by the defaulting member's remaining margin requirements that the firm had kept. The deficiency that would arise in the years 2025 and 2026, according to the firm, would be "negligible" (EUR 1.6 million), and the firm intended to cover this deficiency with its surplus liquidity. Up through the years 2025 and 2026, the margin requirements would completely cover all potential time lags in the cash flow and thus eliminate the risk.

Finansinspektionen makes the overall assessment that during the period in question there has been a remaining credit and market risk that has persisted until the portfolio was transferred in June 2019, ten months after the default event. Comments from Nasdaq Clearing about how it intended to manage the risk and about its interpretation and understanding of the regulatory framework does not justify another assessment.

Investment prohibition is applicable

A central counterparty that wants to apply the exemption from the investment prohibition, as presented above, must cite circumstances showing that the investment has been limited to the period of time required to reduce the credit and market risk to which the central counterparty had been exposed.

Nasdaq Clearing, in this part, has objected with the argument that the firm was waiting for a more beneficial point in time. As presented above, Nasdaq Clearing held the derivative contracts for as long as ten months after the default event. During this entire period, the firm's own resources were exposed to credit and market risk, a risk that typically increases the longer an exposure exists. Given such conditions and since the exemption from the investment prohibition should be applied restrictively, Nasdaq Clearing's objection does not constitute an acceptable explanation.

The exemption from the investment prohibition can also not be applied with a reference to the firm actually keeping the defaulted portfolio during the same period of time, which appears to be Nasdaq Clearing's understanding. It is obviously a conscious decision by the firm not to sell the defaulted portfolio promptly. There is no requirement in EMIR that requires Nasdaq Clearing to keep the defaulted portfolio as long as it did. There has also not been any actual obstacle to closing out the defaulted portfolio earlier. Thus, in this context, it can be noted that the liquidation period that the firm had established for the majority of the derivative contracts that were entered into the defaulting member's clearing account was two to four days. In other words, it would take two to four days to close out the relevant positions in the event of a default.

For these reasons, Nasdaq Clearing has not cited any circumstance that warrants the firm keeping its investment in derivatives for up to ten months after the default event occurred.

Conclusion

Finansinspektionen takes the position that Nasdaq Clearing, by not closing out the derivative contracts until ten months after the default event, disregarded the investment prohibition for derivative contracts in Article 47(1) of EMIR. Through its actions, Nasdaq Clearing exposed both the firm and, by extension, its clearing members to a risk of additional losses. The longer the firm held the positions, the greater the firm's potential risk due to changes in the market and other factors. There is therefore cause to view the course of events seriously.

4.2.5 Mishandled information distribution

According to Article 36(1) of EMIR, a central counterparty, when providing services to its clearing members, and where relevant, to their clients, must act fairly and professionally in accordance with the best interests of its clearing members and clients and in accordance with sound risk management.

In conjunction with the auction in September 2018, Nasdaq Clearing published a number of press releases. The first, which was published at around 11 PM on 12 September 2018, stated in part the following: "The defaulting portfolio has been closed out according to Nasdaq Clearing's close-out procedures and has been fully contained."

In the next press release, published on 19 September 2018, the firm described the course of events during the default event and stated that "the defaulting portfolio was closed out and the risk has been fully contained".

Nasdaq Clearing has stated that the press releases conveyed an accurate depiction to the market and its members. The firm stated in its opinion to Finansinspektionen that the use of the phrase "close out" was a reference to the firm's own procedures and not a reference to the legislation governing the area. In addition, the firm considers that it was correct to state that the portfolio has been "fully contained".

Finansinspektionen does not agree that the press releases conveyed an accurate depiction to the market and its members. Finansinspektionen takes the position that it is clear that "close out" in the context of central counterparty clearing can only be interpreted as an actual close out and sale of the positions in question. Since Nasdaq Clearing used this term in its press releases, the firm has given clearing members and customers cause to believe that the positions in question have been sold. Nasdaq Clearing's objection does not justify any other assessment.

It is naturally of central importance that Nasdaq Clearing, as a systemically important actor, provide correct and accurate information. In order to be able to understand and assess the risks associated with participation in a specific clearing activity, it is very important for clearing members and their clients to receive correct information about the risks the central counterparty has taken on. The incorrect impression from the press releases that the positions had been closed out means, in Finansinspektionen's opinion, that there has been a risk that clearing members and clients were misled about the actual risk conditions that arose given the default event. By not ensuring that the press release gave an accurate depiction of its management, Nasdaq Clearing has therefore clearly disregarded its obligation pursuant to Article 36(1) of EMIR to act fairly and professionally towards its clearing members and clients.

4.2.6 Finansinspektionen's conclusions regarding the management of the default event

Finansinspektionen has observed two breaches linked to Nasdaq Clearing's declaration of default for a clearing member on 11 September 2018.

Nasdaq Clearing disregarded the investment prohibition. The auction in conjunction with the default consisted of a portfolio of derivative contracts that mirrored the market risk in the defaulting member's derivative contracts, not the defaulting member's actual holdings. The defaulted portfolio and the mirror portfolio were not closed out until ten months after the event. Even if Nasdaq Clearing initially acted promptly to limit the immediate financial impact for its members, the firm thereafter allowed a long time to pass before the derivative contracts were closed out. As a result of its management, the firm disregarded

the investment prohibition by keeping a credit and market risk in its operations that a central counterparty should not have.

Finansinspektionen thereby considers there to be cause to view this breach very seriously. By not closing out the positions in derivative contracts promptly enough, Nasdaq Clearing exposed the operations and its members to an unacceptable risk that increased over time since potential credit and market risks typically increase the longer a certain position is held. This thus constitutes a risk that in the long run could have had an impact on financial stability.

Nasdaq Clearing also failed in this part to act fairly and professionally in relation to its members and their clients when incorrectly describing the close out. This action could have had serious repercussions, particularly considering the role of central counterparties in the financial system and that the financial market's participants are dependent on being aware of the risks that they may be exposed to when they engage the central counterparty's services.

5 Configuration error in the margin calculation

As presented above in sections 3.4.1 and 3.4.2, the provisions on margin requirements set out in Article 41 of EMIR constitute a part of the prudential requirements that apply to a central counterparty. The requirement set out in Article 26(2) of EMIR that a company operating a central counterparty must adopt policies and procedures which are sufficiently effective so as to ensure compliance with EMIR are part of the organisational requirements that apply to a central counterparty.

On 26 November 2018, Nasdaq Clearing reported to Finansinspektionen that the firm had identified an error in its calculations of margin requirements. The error was due to an operational mistake that was made in 2015 in the configuration of input data for the parameter calculation application that was used when calculating margin requirements for portfolios containing electricity certificates. Nasdaq Clearing had discovered the error when the incorrect configuration gave rise in November 2018 to obviously incorrect margin requirements compared to the requirement the firm's model, the so-called SPAN model, should have issued.

When the electricity certificate switched its underlying currency in 2015 from EUR to SEK, Nasdaq Clearing did not convert the electricity certificate, which is currently denominated in SEK, back to EUR, thus generating the configuration error. Such a conversion was necessary in order to be able to correctly net this type of contract against Nordic electricity derivatives that were still denominated in EUR.[7] If the amount that is deducted is too large, the result will be a margin requirement that is lower than what it would otherwise be. If the amount that is deducted is instead too small, the result will be a margin requirement that is higher than what it would otherwise be. Due to this error, contracts with different

[7] In order for the netting of two contracts with different underlying currencies to be correct, they first need to be converted to the same currency.

underlying currencies were netted against one another. This resulted in an incorrect net calculation of margin requirements, or, in other words, incorrect netting between contracts. This, in turn, resulted in a risk that the amount deducted from portfolios with electricity certificates and Nordic electricity certificates was incorrect and that the margin requirement thus was different than what it should have otherwise been.

Finansinspektionen has reviewed in this investigation whether the configuration error that Nasdaq Clearing discovered and reported to Finansinspektionen resulted in incorrectly calculated and issued margin calls for its members. Finansinspektionen also investigated whether the firm has had sufficient forms of governance, policies and procedures to be able to prevent the error from occurring.

5.1 Nasdaq Clearing issued insufficient margin calls

Articles 41(1) and 41(2) of EMIR state that a central counterparty must collect sufficient margins and adopt models and parameters to set its margin requirements. The models and parameters must take into account, for example, the risk characteristics of the products cleared. In other words, the rules in EMIR do not predetermine how much margin is to be collected for a certain product; rather, this is determined by the estimated risk and the calculations the central counterparty makes using its models and parameters.

According to Article 24 of RTS 153, the central counterparty has the freedom and the obligation to determine an adequate confidence interval for each class of financial instruments given certain basic requirements that are set out in the article. Article 24(1) sets the lowest level for what the central counterparty can determine is an adequate confidence interval. Article 24(2) contains a list of a number of different factors that the central counterparty must consider when determining an adequate confidence interval. In other words, for each class of financial instruments, a central counterparty must assess whether it requires a higher confidence interval than the lowest level set out by the regulation.

When Nasdaq Clearing reported the configuration error in question to Finansinspektionen, it provided information showing that on 26 November 2018, as a result of the error, it collected margins that were around EUR 50 million to low from its members on the commodities market (calculated using the SPAN model and in accordance with the higher confidence interval of 99.5 per cent that the firm applied at that time). The largest individual deviation for a member amounted on that day to around EUR 42 million.

At the time the configuration error was discovered and for the day for which Nasdaq Clearing had provided data, i.e., 26 November 2018, the firm applied the SPAN model and a confidence interval of 99.5 per cent to the market in question. Nasdaq Clearing, however, disputes that the error constitutes a violation of the regulatory framework, in this case the obligation pursuant to Article 41 of EMIR to call and collect a certain margin amount. The firm takes

the position that it does not matter which model it uses as long as it leads to the firm issuing margin calls that are sufficient for, over an appropriate period of time, covering losses from at least 99 per cent of the exposure movements, which is the lowest level according to Article 24 of RTS 153.

The size of the margin that a central counterparty needs to collect is based on the calculation that the central counterparty makes for each class of financial instruments pursuant to Article 24(2) of RTS 153. This is pursuant to Article 41(1) of EMIR. Finansinspektionen takes the position, therefore, in contrast to Nasdaq Clearing, that it is the model that, pursuant to Article 41(2) of EMIR, the firm submitted to and received approval from Finansinspektionen that determines if the firm met the requirement on collecting sufficient margins.

Finansinspektionen notes that it is not contested that Nasdaq Clearing collected margins on 26 November 2018 that were lower than the amount generated by the SPAN model for which the firm received approval. This already means that the firm at this point in time did not meet the requirement on calls for sufficient margins from its members. Nasdaq Clearing has thereby breached Article 41(1) of EMIR.

5.2 Insufficient governance arrangements, policies and procedures

Articles 26(1) and 26(2) of EMIR state that a central counterparty must have robust governance arrangements that include, for example, effective processes to identify, manage, monitor and report the risks to which a counterparty is or might be exposed, adequate internal control mechanisms and policies and procedures which are sufficiently effective to ensure compliance with EMIR.

Margins constitute an important part of a central counterparty's risk management. It is therefore key that the margin calculations are correct. The risk of operational errors can primarily be managed through sufficient and effective processes and procedures as well as suitable testing procedures. Finansinspektionen thus expects a central counterparty to have policies and procedures that limit the risk of operational errors and perform suitable tests and controls before changes are put into production with the objective of discovering any errors that may have occurred.

It is not contested that Nasdaq Clearing missed an important step in conjunction with electricity certificates switching their underlying currency from EUR to SEK in 2015. This error, up until the point in time when it was discovered and rectified, has meant that there has been a concrete risk that Nasdaq Clearing collected insufficient margins from some members compared to the requirements set out in EMIR. As presented, this risk was also realised given that the firm, at least on 26 November 2018, collected insufficient margins from certain members (see section 5.1).

Nasdaq Clearing has taken the position that it is not possible to determine outright that the firm breached the requirements set out in Article 26 of EMIR

just because there was an error at one point when calibrating a calculation model. According to the firm, this is an approach that in practice would require strict responsibility by the firm since it would mean that the occurrence of an error would immediately lead to the conclusion that the firm also had insufficient methods and procedures. According to the firm, this interpretation of the legislation is too far-reaching.

According to Finansinspektionen, Nasdaq Clearing's position can hardly be perceived as anything other than a way for the firm to try to tone down its responsibility for the error that occurred. Changes that affect the margin model require sufficiently effective controls and tests to discover any potential errors before the change is put into production. Nasdaq Clearing should have realised that the change in question would affect the netting and thus the margin requirements. The firm, therefore, should have verified that it was using correct input data and checked whether backtesting to the same underlying portfolios gave conflicting results. Through effective procedures and policies, combined with suitable controls and testing, an operational error of the character in question could have been avoided.

Finansinspektionen, as part of the investigation, requested to see the procedures Nasdaq Clearing had in place at the time of the configuration of input data in 2015. In its response to Finansinspektionen, the firm briefly stated that there were procedures for the configuration of input data when the error occurred in 2015. The firm has stated that the responsible group at the time in question consisted of two specialists who managed the relevant models and – in terms of duality – that there was a procedure under which these two persons performed controls of each other's work. The firm has not saved any written documentation describing this procedure.

Finansinspektionen notes that Nasdaq Clearing's brief response to the question about which procedures the firm had in 2015 is the information the authority has to work with when determining which methods and procedures the firm had in place that year. The firm has not described what the procedure for configuration entailed at this point in time other than that the two people who worked with it checked each other's work. The firm has also not asserted that it conducted any actual testing or controls in conjunction with the configuration of input data (besides *backtesting*).

According to Finansinspektionen, the investigation shows that Nasdaq Clearing did not have satisfactory methods and procedures to prevent a configuration error from occurring. The firm therefore has not met the requirements set out in either Article 26(1) or 26(2) of EMIR. The configuration error resulted in incorrect margin calculations and the firm collecting insufficient margins on at least one occasion. Finansinspektionen would also like to note in this context that well-functioning procedures and guidelines for calculating margin requirements are a prerequisite for a central counterparty to be able to follow other provisions of the regulatory framework, for example the requirement that a central counterparty must save and update information about, for example,

positions and margin requirements for ten years (Article 29 of EMIR and Article 14 of RTS 153).

5.3 Finansinspektionen's conclusions regarding the margin calculation

Finansinspektionen has been able to determine that Nasdaq Clearing violated the regulatory framework associated with the calculation of the margin requirement by having issued an insufficient margin call on at least one occasion and not having satisfactory methods and procedures for preventing the configuration error from occurring. Finansinspektionen takes the position that there has been a risk that the firm issued insufficient margin calls during the entire time the error persisted.

Since the deficiencies resulted in the firm in actuality collecting insufficient margins, Finansinspektionen takes a serious view of this matter. This applies in particular given the systemically important position that Nasdaq Clearing holds in the financial system. Calculating and requiring margins constitutes one of the pillars of a central counterparty's operations. When Nasdaq Clearing makes changes that could affect the margin model, Finansinspektionen expects the firm to conduct thorough and appropriate controls and tests with the objective of discovering any errors before the change is taken into production. Nasdaq Clearing has not done this, and the firm has also not had sufficient policies and procedures to discover the configuration error that was made in 2015.

6 Consideration of intervention

6.1 Applicable provisions

6.1.1. EMIR

Pursuant to Article 20(1)(d) of EMIR, Finansinspektionen, without prejudice to Article 22(3) of EMIR, must withdraw the central counterparty's authorisation if it has seriously and systematically infringed on any of the requirements laid down in EMIR.

According to the first paragraph of Article 22(3) of EMIR, each Member State must ensure that appropriate administrative measures, in conformity with national law, can be taken or imposed against the natural or legal persons if they do not comply with EMIR. These measures, pursuant to the second paragraph of the same article, must be effective, proportionate and dissuasive and may include requests for remedial action within a set time frame.

6.1.2 Securities Market Act

According to Chapter 1, section 1a of the Securities Market Act, clearing operations that consist of entering as a counterparty to both buyers and sellers of financial instruments are only subject to Chapter 25, section 1, section 2, second

paragraph, and sections 6, 8–11, 17, 25–28, and 29 with regard to interventions and Chapter 26, section 1 of the same Act with regard to appeals.

According to Chapter 25, section 1, Finansinspektionen shall intervene, for example, where a Swedish clearing organisation has breached its obligations pursuant to this act, other regulations that govern the firm's operations, the firm's articles of association, statutes or rules, or internal instructions which are based on a legislation that governs the firm's operations. Finansinspektionen shall then issue an order to limit or reduce the risks in the business in some respect within specific time, limit or preclude in full payment of dividends or interest, or take another measure to rectify the situation, issue an injunction against executing resolutions, or issue a remark. Where the infringement is serious, the authorisation of the firm shall be withdrawn or, if sufficient, a warning issued.

According to Chapter 25, section 2, second paragraph, Finansinspektionen may refrain from intervening if the infringement is negligible or excusable, if the firm rectifies the matter or if any other authority or any other body has taken action against the firm and such action is deemed sufficient.

If a Swedish clearing organisation is notified of a decision regarding a remark or warning in accordance with Chapter 25, section 1, Finansinspektionen, according to Chapter 25, section 8, may decide that the firm shall pay an administrative fine.

Chapter 25, section 9 specifies the limits for the size of the administrative fine. According to this provision, the administrative fine for a Swedish clearing organisation may be set at the most to the highest of

1. an amount as per 2 July 2014 in SEK corresponding to EUR five million,
2. ten per cent of the firm's turnover or, where applicable, corresponding turnover at the group level for the immediately preceding financial year, or
3. two times the profit recorded by the firm as a result of the infringement, if the amount can be determined.

The administrative fine may not be set at an amount smaller than SEK 5,000. When determining the size of the administrative fine, according to Chapter 25, section 10, special consideration shall be given to such circumstances as those set out in sections Chapter 25, sections 2 and 2a, the firm's financial position, and the profit the firm realised as a result of the regulatory infringement, if such can be ascertained.

6.2 Nasdaq Clearing's position

Nasdaq Clearing has objected to an intervention on the grounds that there is no legislative basis for such an action since the legislation in the matter at hand is not sufficiently clear. Nasdaq Clearing has also stated that the participation requirements were reviewed and approved by Finansinspektionen as part of the

annual review that is conducted pursuant to Article 21 of EMIR. Intervening against the deficiencies in the participation requirements, therefore, according to the firm, is not possible given general administrative principles.

Nasdaq Clearing has referred furthermore to the measures the firm has taken as a result of the default event and the deficiencies that Finansinspektionen identified as part of the investigations that are relevant in this decision.

Nasdaq Clearing has stated that, after the default event, it initiated a review of the firm's risk framework that resulted in an action plan, "Risk Management Enhancement Program" (RMEP). Nasdaq Clearing also stated that Finansinspektionen's investigations have been an important part of this work and that the investigations largely confirmed the conclusions that firm drew itself after the default event and that are now are the focus of RMEP. According to Nasdaq Clearing, the investigations also helped the firm identify additional improvement opportunities – in addition to those identified during the firm's own investigation – that the firm has since implemented. The firm has also partially reassessed its opinion and agrees with Finansinspektionen that there was room for improvement in some points.

Nasdaq Clearing, with regard to the investigation into the participation requirements, has asserted that there has been significant room for improvement of the firm's requirements, procedures and documentation in several respects. Therefore, both the financial and the operational admission criteria have been enhanced, concretised, and supplemented with guidelines on the firm's website that further clarify and concretise the requirements in a transparent manner. The firm also removed the exemption possibility from the admission criteria and changed the clearing rules so that private individuals may no longer be allowed as members.

Despite its position on the matter, Nasdaq Clearing has reworked the requirements that refer to operational capacity. As a result, the requirements are more concrete and stricter with regard to a potential member's organisation. The firm also published guidelines on its website that clarify and concretise operational requirements and how they are applied.

With regard to the obligation to require sufficient financial resources, Nasdaq Clearing has stated that measures were taken to strengthen these requirements. The firm has raised the minimum capital requirements for some member categories, introduced exposures limits, and developed and implemented a minimum level for credit assessments.

With regard to the obligation to monitor compliance with the admission criteria on an ongoing basis, Nasdaq Clearing has stated that it does not consider its structure at the time to be in conflict with EMIR, but it shares Finansinspektionen's assessment that the ongoing controls can be improved. The firm has therefore implemented a number of measures, which, in addition to the exposure limits mentioned above, include clarifying the members' notification

obligation and introducing quarterly data collection from members. For members assessed to entail an elevated risk, data is collected monthly.

With regard to the measures the firm has taken for the annual review of the members' compliance with the admission criteria, the firm has referred to the so-called due diligence form it has used since Q4 2018.

With regard to the investigation of the discovered configuration error, Nasdaq Clearing stated in its opinion that it views the event that occurred very seriously. The firm has taken measures to try to prevent similar errors and developed its testing framework to minimise the risk that it does not discover errors at an early stage.

6.3 The breaches require intervention

Finansinspektionen's investigations show that there have been significant deficiencies in how Nasdaq Clearing has followed the organisational, business conduct and prudential requirements that apply to a central counterparty. The observed deficiencies have meant that Nasdaq Clearing has disregarded its central obligations under EMIR that aim to manage the risks arising from systemically important clearing operations.

Nasdaq Clearing has objected with the argument that the legislation is not sufficiently clear for Finansinspektionen to be able to intervene. This objection is remarkable coming from an actor that must manage the risks associated with systemically important clearing operations. It is Finansinspektionen's decided opinion that the requirements placed on Nasdaq Clearing are set out in laws that meet requisite demands on clarity and predictability, in particular with regard to legislation targeting professional actors who are expected to be able to become familiar with and apply the high-level requirements set out by the regulation. What Nasdaq Clearing is objecting to can therefore be disregarded.

Nasdaq Clearing has also asserted that Finansinspektionen, as part of the review that is conducted pursuant to Article 21 of EMIR, has reviewed and approved parts of the operations that are the subject of this decision, and for this reason the authority cannot intervene in these parts. Finansinspektionen does not agree with this assessment. Pursuant to Article 21(3) of EMIR, the competent authority, in this case Finansinspektionen, determines the scope of the annual review required under the regulation. According to Finansinspektionen, the review that Nasdaq Clearing is referring to has been designed and limited in such a manner that it has not resulted in any position-taking or decisions from the authority that prevents the investigations in question to lead to an intervention. Therefore, the previous review does not prevent Finansinspektionen from intervening against the observed deficiencies.

Given an overall assessment, it is obvious that the breaches are not negligible or excusable. There are therefore grounds for intervening against Nasdaq Clearing. The information that Nasdaq Clearing has now taken measures to rectify some of the deficiencies does not justify any other assessment.

6.4 Choice of intervention

6.4.1 Nasdaq Clearing shall receive a warning

Finansinspektionen notes that the investigations show that Nasdaq Clearing has had significant deficiencies in the firm's core business. As presented above, these deficiencies could be linked to more or less all categories of safe and sound requirements in the regulatory framework. This already implies that the breaches should be viewed as serious.

The rules that Nasdaq Clearing has violated are crucial for a central counterparty's ability to adequately manage the risks in its operations. Both the disregard of the investment prohibition after the default event and the configuration error in the margin calculation clearly show that Nasdaq Clearing has been exposed to prohibited risks. But the deficient participation requirements are clearly also an aggravating circumstance since they show that Nasdaq Clearing basically did not have fundamental insights into the need to take sufficient measures to ensure that its members are able, for example, to meet margin calls and contribute to the default fund. Together with the other deficiencies described in this decision, these breaches have posed major risks to the financial system – which the default event in September 2018 shows in particular. Through these breaches, Nasdaq Clearing also risked damaging the public confidence in the clearing operations. This justifies a stringent assessment.

In summary, Finansinspektionen makes the assessment that the breaches entail that Nasdaq Clearing has seriously violated several fundamental requirements set out in EMIR. The firm has disregarded organisational, business conduct and prudential requirements, in other words all of the aspects of the requirements on the operations that are governed by EMIR, with the exception of some provisions regarding calculations and reporting. The breaches in question are so serious that there are grounds to consider an intervention through which Nasdaq Clearing is no longer able to conduct its operations. However, this kind of measure is very far-reaching and must be weighed against, for example, Nasdaq Clearing's initiation of measures, and plans to implement additional measures, that significantly reduce the risk of new or similar regulatory infringements (cf. Bill 2006/07:115 p. 499). Given an overall assessment, Finansinspektionen therefore takes the position that a warning is sufficient as a sanction.

6.4.2 Warning will be accompanied by an administrative fine

An intervention, in addition to being effective and proportionate, must also be dissuasive. The warning Finansinspektionen is issuing Nasdaq Clearing, therefore, will be accompanied by an administrative fine.

The lowest statutory administrative fine is SEK 5,000.

Finansinspektionen must establish the highest allowable amount for the administrative fine ("the ceiling" for the administrative fine) based on the conditions that apply on a case-by-case basis. It has not been possible to determine if there are any profits, or in such case their size, that are attributable to Nasdaq Clearing or the costs the firm avoided as a result of the regulatory violations. A ceiling for the administrative fine determined by the firm's, or the group's, turnover in this decision (see below) will exceed an amount corresponding to EUR 5 million. The ceiling for the administrative fine will therefore be based on turnover.

The administrative fine thus may amount to at the most ten percent of the firm's or, where applicable, the group's turnover for the immediately preceding financial year. Since Nasdaq Clearing is part of a group, it is the group's turnover that sets the ceiling. As a basis for its assessment, Finansinspektionen has therefore used the consolidated financial statements for Nasdaq, Inc. Nasdaq Clearing's net turnover in the most recently available annual report for 2019 amounted to SEK 563 million, while the corresponding turnover at the consolidated level amounted to USD 4,262 million, which translates into approximately SEK 40,320 million using the dollar's average exchange rate[8]. The ceiling for the administrative fine therefore amounts to around SEK 4,302 million, which corresponds to ten per cent of consolidated turnover.

The administrative fine thereby shall be set between SEK 5,000 and SEK 4,032 million.

The size of the administrative fine can be seen as a gradation of the violations. When Finansinspektionen determines the size of the administrative fine, the authority must take into account the seriousness of the violations and their duration. Special consideration must be given to the nature of the violations, their tangible and potential effects on the financial system, losses incurred and the degree of responsibility. The administrative fine must be effective, dissuasive and proportionate.

When determining the size of the administrative fine, consideration must also be given to the general increase in the administrative fines issued in recent years and that the size of the consolidated turnover shall now be considered in the assessment. The fine should also not be set at such as level as to threaten the financial position of the firm in question.

[8] In this calculation, Finansinspektionen used an average exchange rate for the US dollar of SEK 9.46.

Finansinspektionen has outlined in the previous sections its assessment of the breaches. The circumstances that have been presented in the discussion of whether or not to intervene are also those that should be taken into consideration when the authority determines the size of the administrative fine. Given to the above presentation, Finansinspektionen notes that there are a number of aggravating circumstances and the committed breaches are serious. According to Finansinspektionen, they clearly show that Nasdaq Clearing has neglected to ensure that its operations are conducted in accordance with applicable regulations in central areas. Nasdaq Clearing has underestimated in particular its role as a systemically important actor in the financial system by taking unacceptable risks, which by extension could have resulted in a threat to financial stability, and not just in Sweden. This is clearly an aggravating circumstance when determining the administrative fine.

In this context, Finansinspektionen would like to highlight in particular the prohibited risk that Nasdaq Clearing took when managing the default event by exposing its own resources to a credit and market risk by, in violation of the regulations, disregarding the investment prohibition in EMIR for a not insignificant amount of time. The fact that the default event related to a relatively minor clearing member but still had very serious economic impacts clearly shows that the potential effects on the financial system from these breaches could have been significant.

With reference to that presented above and that the administrative fine must be dissuasive and proportionate in relation to the seriousness of the breaches, the administrative fine must in this case be set at a significantly higher amount than what would have been the case if Nasdaq Clearing had not been a part of a group. This applies in particular since the breaches have been committed in a systemically important smaller firm that is part of a large group with significant influence on the infrastructure in the financial markets.

As stated above, the ceiling for the administrative fine in this case is around SEK 4,032 million. This justifies that the administrative fine, following an overall assessment, being set at SEK 300 million. Finansinspektionen has then also taken into account the measures Nasdaq Clearing has undertaken to implement and that Nasdaq Clearing has a turnover of SEK 563 million and easily meets the capital requirements on around SEK 650 million that the firm must have pursuant to EMIR.

The administrative fine will be invoiced by Finansinspektionen after the decision enters into force.

FINANSINSPEKTIONEN

Sven-Erik Österberg

Chairman of the Board of Directors

Magnus Schmauch
Advisor

The decision in this matter was made by the Board of Directors of Finansinspektionen (Sven-Erik Österberg, Chair, Maria Bredberg Pettersson, Peter Englund, Astri Muren, Stefan Nyström, Mats Walberg and Charlotte Zackari) following a presentation by Senior Advisor Magnus Schmauch. Chief Legal Counsel Eric Leijonram, Executive Director Malin Omberg, Acting Deputy Head of Department Anna Svensson and Deputy Head of Department Andreas Heed participated in the final proceedings.

Appendices

Appendix 1 – How to appeal
Appendix 2 – Applicable provisions

Copy: Nasdaq Clearing Aktiebolag's CEO

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N O T I F I C A T I O N R E C E I P T

FI Ref. 18-23053
FI Ref. 18-23054
FI Ref. 18-24342
Notification No. 1

Document:

Decision regarding a warning and administrative fine for Nasdaq Clearing Aktiebolag, announced on **27 January 2021**

I have received the document on this date in my capacity as signatory for the firm.

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DATE

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NEW ADDRESS (IF APPLICABLE)

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This receipt must be returned to Finansinspektionen **immediately**. If the receipt is not returned, the notification may be issued in another manner, e.g., via a court officer.

If you use the enclosed envelope, there is no charge for returning the receipt.

Do not forget to **specify the date of receipt**.

How to appeal

It is possible to appeal the decision if you consider it to be erroneous by writing to the Administrative Court. Address the appeal to the Administrative Court in Stockholm, but send the appeal to Finansinspektionen, Box 7821, 103 97 Stockholm or finansinspektionen@fi.se.

Specify the following in the appeal:

- Name, personal ID number or corporate ID number, postal address, email address and telephone number
- The decision you are appealing against and the case number
- What change you would like and why you believe the decision should be changed.

If you engage an agent, specify the name, postal address, email address and telephone number of the agent.

Finansinspektionen must receive the appeal within three weeks from the day you received the decision.

If the appeal was received on time, Finansinspektionen will assess whether the decision will be changed and then send the appeal, the documents in the appealed matter and the new decision, if relevant, to the Administrative Court in Stockholm.

Appendix 2

Applicable provisions

Review

Article 21(1) of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR) states that the competent authorities referred to in Article 22 shall review the arrangements, strategies, processes and mechanisms implemented by central counterparties to comply with this regulation and evaluate the risks, including at least financial and operating risks, to which these central counterparties are, or might be, exposed.

Article 21(3) of EMIR states that the competent authorities shall establish the frequency and depth of the review and evaluation referred to in paragraph 1 having regard to the size, systemic importance, nature, scale, complexity and links to other financial market infrastructure at the central counterparty in question. The review and evaluation shall be updated at least on an annual basis.

Organisational requirements

Article 26(1) of EMIR states that a central counterparty shall have robust governance arrangements, which include a clear organisational structure with well-defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks to which it is or might be exposed, and adequate internal control mechanisms, including sound administrative and accounting procedures.

Article 26(2) of EMIR states furthermore that a central counterparty shall adopt policies and procedures which are sufficiently effective so as to ensure compliance with EMIR, including compliance of its managers and employees with all the provisions of EMIR.

Conduct of business rules

EMIR

According to Article 36(1) of EMIR, a central counterparty, when providing services to its clearing members, and where relevant, to their clients must act fairly and professionally in accordance with the best interests of its clearing members and clients and sound risk management.

Article 37(1) of EMIR states that a central counterparty shall establish, where relevant per type of product cleared, the categories of admissible clearing members and the admission criteria, upon the advice of the risk committee pursuant to Article 28(3). Such criteria shall be non-discriminatory, transparent and objective so as to ensure fair and open access to the central counterparty

and shall ensure that clearing members have sufficient financial resources and operational capacity to meet the obligations arising from participation in a central counterparty. Criteria that restrict access shall be permitted only to the extent that their objective is to control the risk for the central counterparty.

Article 37(2) of EMIR states that a central counterparty shall ensure that the application of the criteria referred to in paragraph 1 is met on an ongoing basis and shall have timely access to the information relevant for such assessment. A central counterparty shall conduct, at least once a year, a comprehensive review of compliance with this Article by its clearing members.

Prudential requirements

EMIR

Article 41(1) of EMIR states that a central counterparty shall impose, call and collect margins to limit its credit exposures from its clearing members and, where relevant, from central counterparties with which it has interoperability arrangements. Such margins shall be sufficient to cover potential exposures that the central counterparty estimates will occur until the liquidation of the relevant positions. They shall also be sufficient to cover losses that result from at least 99 per cent of the exposures movements over an appropriate time horizon, and they shall ensure that a central counterparty fully collateralises its exposures with all its clearing members, and, where relevant, with central counterparties with which it has interoperability arrangements, at least on a daily basis. A central counterparty shall regularly monitor and, if necessary, revise the level of its margins to reflect current market conditions taking into account any potentially procyclical effects of such revisions.

Article 41(2) of EMIR states that, in order to calculate the margin requirements, the central counterparty shall adopt models and parameters in setting its margin requirements that capture the risk characteristics of the products cleared and take into account the interval between margin collections, market liquidity and the possibility of changes over the duration of the transaction. The models and parameters shall be validated by the competent authority and subject to an opinion in accordance with Article 19.

Article 47(1) of EMIR states that a central counterparty shall invest its financial resources only in cash or in highly liquid financial instruments with minimal market and credit risk. A central counterparty's investments shall be capable of being liquidated rapidly with minimal adverse price effect.

Article 48(2) of EMIR states that a central counterparty shall take prompt action to contain losses and liquidity pressures resulting from defaults and shall ensure that the closing out of any clearing member's positions does not disrupt its operations or expose the non-defaulting clearing members to losses that they cannot anticipate or control.

RTS 153

The general requirements on margins set out in Article 41 of EMIR are clarified in Articles 24–26 of Commission Delegated Regulation (EU) No 153/2013[9] (RTS 153).

Article 24(1) of RTS 153 states that a central counterparty shall calculate the initial margins to cover the exposures arising from market movements for each financial instrument that is collateralised on a product basis, over the time period defined in Article 25 and assuming a time horizon for the liquidation of the position as defined in Article 26. For the calculation of initial margins, the central counterparty shall at least respect the following confidence intervals:

a) for OTC derivatives, 99.5%;

b) for financial instruments other than OTC derivatives, 99%.

Article 24(2) of RTS 153 states that, for the determination of the adequate confidence interval for each class of financial instruments it clears, a central counterparty shall in addition consider at least the following factors:

a) the complexities and level of pricing uncertainties of the class of financial instruments which may limit the validation of the calculation of initial and variation margin;

b) the risk characteristics of the class of financial instruments, which can include, but are not limited to, volatility, duration, liquidity, non-linear price characteristics, jump to default risk and wrong way risk;

c) the degree to which other risk controls do not adequately limit credit exposures;

d) the inherent leverage of the class of financial instruments, including whether the class of financial instrument is significantly volatile, is highly concentrated among a few market players or may be difficult to close out.

The rules on investments are governed in addition by Articles 43–46 of RTS 153 and Annexes I and II of RTS 153. Whereas point 47 of RTS 153 states that provisions entail an investment prohibition with regard to derivatives. Annex II of RTS 153 states that for the purposes of Article 47(1) of EMIR, financial instruments can be considered highly liquid financial instruments, bearing minimal credit and market risk, if they meet the conditions listed there. Point 2 of Annex II of RTS 153 states that derivative contracts can also be considered highly liquid financial investments, bearing minimal credit and market risk if they are entered into for the purpose of:

a) hedging the portfolio of a defaulted clearing member as part of the central counterparty's default management procedure; or

[9] Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on requirements for central counterparties, in its wording after 16 June 2016.

b) hedging currency risk arising from its liquidity management framework established in accordance with Chapter VIII.

Where derivative contracts are used in such circumstances, their use shall be limited to derivative contracts in respect of which reliable price data is published on a regular basis and to the period of time necessary to reduce the credit and market risk to which the central counterparty is exposed.