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EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT

Accompanying the documents

Proposal for a
REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
amending Regulations (EU) No 648/2012, (EU) No 575/2013 and (EU) 2017/1131 as regards measures to mitigate excessive exposures to third-country central counterparties and improve the efficiency of Union clearing markets

and

Proposal for a
DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
amending Directives 2009/65/EU, 2013/36/EU and (EU) 2019/2034 as regards the treatment of concentration risk towards central counterparties and the counterparty risk on centrally cleared derivative transactions

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Need for action

EU financial markets are critically dependent on some services provided by certain third-country central counterparties (CCPs), leading to significant financial stability risks for the EU. The United Kingdom (UK) is the main location for clearing euro-denominated derivatives, with a market share of more than 90%. The European Central Bank (ECB) and the Commission identified clearing as a significant financial stability risk for the EU if EU market participants were to abruptly lose access to UK CCPs. This resulted in the adoption of an equivalence decision in September 2020. In this decision, the Commission reiterated the message to EU market participants to reduce their excessive exposures to CCPs established in the UK. Such reduction however has not happened to date.

Engagement with relevant EU bodies such as the European Securities and Markets Authority (ESMA), the ECB, the European Systemic Risk Board and the Single Supervisory Mechanism, within an ad-hoc working group on clearing established by the Commission, confirmed the existence of the problem and its risks for financial stability. Discussions within the working group have led to conclude that significantly reducing those excessive exposures in an orderly and controlled manner would necessitate a combination of legislative and non-legislative changes in the years to come. These changes would be needed to: (i) improve the attractiveness of clearing in the EU; (ii) encourage infrastructure development in the EU; and (iii) enhance supervisory arrangements in the EU in order to ultimately address relevant financial stability risks.

Without further EU action, market participants will very likely continue to clear in those systemic third-country CCPs, thus maintaining, even increasing, the over-reliance described. This carries significant financial stability risks in case of a stress-scenario involving a third-country CCP or in case of a sudden loss of access to its services.

Possible solutions

Available policy options were identified on the basis of ESMA’s 2021 report assessing systemically important UK CCPs, the discussions with the above EU bodies and in the working group on clearing and a targeted public consultation. The measures considered in the impact assessment aim to address problems on both the supply and demand side as well as the increasing EU cross-border risks which arise as a consequence of growing EU clearing flows.

On the supply side, in order to improve the attractiveness of CCPs located in the EU for market participants, several options are considered to streamline the procedures or introduce a simplified mechanism allowing CCPs to make changes on their models and parameters in a swift and business friendly way.

On the demand side, in order to encourage clearing in EU CCPs, several options are considered: one disincentivising banks’ excessive exposures to CCPs, one requiring market participants to maintain an active account at EU CCPs, one broadening the scope of entities clearing in the EU, one facilitating access to clearing for clients and indirect participants, and a combination of these options.

Finally, in order to strengthen the framework for EU CCP supervision to better take into account cross-border risks, thus ensuring financial stability, two options are considered, one streamlining the supervisory framework and introducing joint supervisory teams under the responsibility of the national supervisors, and the other creating a single supervisor for EU CCPs.

Several options were discarded in the first stage, notably mandating clearing in the EU or requiring that the clearing obligation be fulfilled in EU CCPs or less risky third-country CCPs. The following options were also discarded in the first stage: granting all EU CCPs access to central bank facilities, extending the Target 2 operating hours and broadening the scope of the clearing obligation.

Impacts of the preferred option

The analysis selected preferred options based on their contribution to specific objectives of this initiative which are to: (i) improve the attractiveness of EU CCPs, (ii) encourage clearing in EU CCPs, and (iii) allow for a stronger consideration of cross-border risks, as well as their cost-effectiveness and coherence.

On the supply side, a combination of streamlined procedures and an ex-post validation mechanism was selected as the preferred option. This would allow to achieve simplification of the current procedures to the greatest extent possible while preserving financial stability. The assessment concludes that this combination would be best suited to achieve the first specific objective (improving the attractiveness of EU CCPs). As regards the second specific objective of encouraging clearing in the EU, this option could indirectly contribute to it by increasing the attractiveness of CCPs located in the EU for market participants. At the same time, it would reduce administrative and opportunity costs for EU CCPs more than either option considered in isolation.

On the demand side, the preferred option combines limiting banks' excessive exposures to CCPs, requiring the establishment of an active account, broadening the scope of market participants clearing in the EU and facilitating clearing by clients in order to remove obstacles to clearing by market participants that usually clear as clients. This will help address the over-reliance on third-country systemically important CCPs. It would achieve the specific objective of enhancing clearing in the EU more than each option considered individually and would strike a good balance between attaining the objective and limiting negative impacts on the market. It would clearly establish a requirement for increasing clearing volumes in EU CCPs, through the active account measure. At the same time, it would establish a credible framework for ensuring compliance by banks and investment firms – which are the most important financial counterparties. This option is considered the most suitable and feasible, as it is expected to avoid disruptive impacts on the competitiveness of EU clearing members and could be adapted and calibrated to take into account cost impacts for smaller clients, while allowing for a gradual reduction in exposures to systemically important CCPs, thus reducing the risks for the EU's financial stability.

With regards to supervision, based on the assessment and comparison of all options, the analysis shows that targeted amendments to the current supervisory framework are likely to be the most proportionate approach, albeit not necessarily being the most effective option for strengthening the consideration of cross-border risks. This option also considers concerns that more centralised CCP supervision at EU level would not be consistent with the ultimate responsibility for potentially supporting a CCP in a crisis, which under the CCP Recovery and Resolution Regulation remains with each CCP's Member State of establishment.

In terms of costs, while financial stability is a public good and therefore not quantifiable, the options retained can be calibrated to ensure that costs to market participants, CCPs, ESMA and national authorities are proportionate.