EMIR and ESMA Regulations: procedures and authorities involved for the authorisation of CCPs and requirements for the recognition of third-country CCPs

2017/0136(COD) - 13/06/2017 - Legislative proposal

PURPOSE: to strengthen the supervision of CCPs in the EU and third countries with a view to consolidating the financial stability of the European Union (EU).

PROPOSED ACT: Regulation of the European Parliament and of the Council.

ROLE OF THE EUROPEAN PARLIAMENT: the European Parliament decides in accordance with the ordinary legislative procedure and on an equal footing with the Council.

BACKGROUND: following the financial crisis, and in line with the commitment made at the 2009 G20 in Pittsburgh, the EU adopted Regulation (EU) No 648/2012 of the European Parliament and of the Council on European market infrastructures (EMIR) to reduce systemic risk associated with the significant use of derivatives in order to preserve financial stability.

The EMIR contains several measures to ensure that standardised over-the-counter (OTC) derivatives contracts are cleared through a Central Counterparty (CCP). It introduces strict prudential, organisational and business conduct requirements for CCPs and established arrangements for their prudential supervision to minimise any risk to users of a CCP and underpin systemic stability.

There are currently **17 central counterparties established in the EU**, all of which are approved under EMIR to offer their services within the Union, although not all of them are authorised to clear all asset classes (e.g. only 2 CCPs clear credit derivatives, only 2 CCPs clear inflation derivatives). An additional **28 third-country CCPs** have been recognised under EMIR's equivalence provisions, allowing them to offer their services in the EU.

Under EMIR, EU CCPs are supervised by colleges of national supervisors, the **European Securities and Markets Authority** (ESMA), relevant members of the European System of Central Banks (ESCB), and other relevant authorities.

Since the adoption of EMIR, **the volume of CCP activity** – in the EU and globally - **has grown rapidly** both in scale and in scope. As of end of June 2016, around 62% of the global value of all OTC derivatives contracts and asset classes (interest rates, credit default, foreign exchange, etc.) were centrally cleared by CCPs, which is equivalent to $337 trillion.

The **growing importance of CCPs** in the financial system and the associated concentration of credit risk in these infrastructures have drawn the attention of governments, regulators, supervisors, central banks and market participants.

The Commission therefore considers that **further reforms to harmonise and strengthen the monitoring of EU and third country CCPs** are now necessary.

The proposal is in line with the Commission proposal for a Regulation on CCP Recovery and Resolution in November 2016. It complements the Commission's proposal for targeted amendments to EMIR which seeks to simplify certain EMIR requirements and make them more proportionate in order to reduce excessive costs for market participants, without compromising financial stability. This proposal should therefore provide further incentives for market participants to use central clearing – again reinforcing the importance of CCPs within the financial system.

It also takes into account feedback received following the publication of the Commission's Communication on responding to challenges for critical financial market infrastructures.

The objective of the proposal is to ensure that authorities are appropriately prepared to address a failing CCP, safeguarding financial stability and limiting taxpayer costs. The CCP Recovery and Resolution proposal refocused attention on the supervisory arrangements for EU and third country CCPs included in EMIR and the extent to which these arrangements can be made more effective five years after adoption of EMIR. This proposal is currently under negotiations in the European Parliament and the Council. That ongoing work-stream needs to be coordinated and consistent with the current proposal.

IMPACT ASSESSMENT: the preferred options in the impact assessment relate to targeted amendments of the of the supervisory arrangements of EMIR applying both to CCPs established in the EU and to third-country CCPs with a view to:

- **enhancing the supervision of CCPs established in the EU**: the current supervisory arrangements should be streamlined and further centralised through the establishment of a European supervisory mechanism, ensuring the proper involvement of national authorities, central banks of issue and ESMA within the scope of their responsibilities;
- **enhancing supervisory arrangements within the EU designed to mitigate the risks related to third-country CCPs**: these CCPs could be subject to a ‘sliding scale’ of additional supervisory requirements by ESMA and relevant CBIs based on objective criteria or thresholds.

CONTENT: this proposal aims to introduce specific amendments to the EMIR and ESMA regulations with a view to **establishing a clear and coherent supervisory arrangements for CCPs** established in the EU and in third countries.

The objective is to ensure that the EU authorities and national authorities are able to cope with a failing CCP, maintain financial stability and avoid that costs associated with the restructuring and the resolution of failing CCPs fall on taxpayers.

The main elements of the proposal are:

Creation of a new supervisory mechanism: the proposal also ensures closer cooperation between supervisory authorities and central banks responsible for EU currencies. To achieve this, a **newly-created supervisory mechanism will be established within European Securities and Markets Authority** (ESMA) ('CCP Executive Session') which will be responsible for ensuring a more coherent and consistent supervision of EU CCPs as well more robust supervision of CCPs in non-EU countries, or 'third countries'.

The proposed amendments focus on (i) the accountability and independence of the members of the CCP Executive Session; (ii) the interactions between the CCP Executive Session and the tasks of the Executive Director of ESMA; (iii) strengthening ESMA's information-gathering capacity; and (iv) the conditions and procedures for the authorisation and the supervision of the CCPs established in the Union.

Third country central counterparties: the proposal aims to make the process of recognition and supervision of third country CCPs stricter for those countries which are of systemic importance to the EU.

The proposal introduces a new "two tier" system for classifying third-country CCPs. Non-systemically important CCPs (Tier 1) will continue to be able to operate under the existing EMIR equivalence framework.

However, **systemically important CCPs** (so-called Tier 2 CCPs) **will be subject to stricter requirements**. These requirements include:

- compliance with the necessary prudential requirements for EU-CCPs while taking into account third-country rules;
- confirmation from the relevant EU central banks that the CCP complies with any additional requirements set by those central banks (e.g. the availability or type of collateral held in a CCP, segregation requirements, liquidity arrangements, etc.);
- the agreement of a CCP to provide ESMA with all relevant information and to enable on-site inspections, as well as the necessary safeguards confirming that such arrangements are valid in the third country.

In the event that certain CCPs may be of particular systemic importance for the EU financial system, the Commission could, at the request of ESMA and in agreement with the relevant central bank, decide that a CCP will only be able to provide services in the Union if it establishes itself in the EU.

BUDGETARY IMPLICATION: the impact of the legislative proposal on expenditure is as follows: (i) the hiring of 47 new temporary staff at ESMA (from August 2018); (ii) the cost of these new temporary agents will be fully financed by the fees raised from industry (no impact on the EU budget).

As ESMA would however incur costs under the Regulation from the entry into force of the Regulation, there is a need to obtain additional budget from the EU in 2018 and 2019 in order to cover for at least the 12 first months of operations following the entry into force of the Regulation.

The estimated impact on expenditure is estimated at **EUR 4 310 555 in 2018 and EUR 7 788 789 in 2019**.

DELEGATED ACTS: the proposal contains provisions empowering the Commission to adopt delegated acts in accordance with Article 290 of the Treaty on the Functioning of the EU.