

PUBLIC STATEMENT

ESMA concludes Tier 2 CCP assessment under Article 25(2c) of EMIR

The European Securities and Markets Authority (ESMA) conducted a comprehensive assessment of systemically important Third-Country Central Counterparties (Tier 2 CCPs) established in the United Kingdom (UK), and of the risks they may pose to the financial stability of the European Union (EU) or one of its Member States. The CCPs concerned are LCH Ltd and ICE Clear Europe Ltd.

The aim of the assessment was to determine the risks posed by a CCP to the financial stability of the EU, or one of its Member States, even if that CCP was to comply fully with the conditions for recognition as a Tier 2 CCP, as well as to consider the costs, benefits and consequences of a potential decision not to recognise the CCP or some of its clearing services, as required by Article 25(2c) of Regulation 648/2012 (EMIR).

Based on its assessment, ESMA concludes that it will not recommend to the European Commission to derecognise a Tier 2 CCP, or one of its services, at this point in time. Instead, ESMA is proposing that measures be considered by the relevant EU institutions and authorities to mitigate risks related to the Tier 2 CCP clearing services that have been identified as being of substantial systemic importance for the EU. The assessment was subject to a consultation of the European Systemic Risk Board and the relevant Central Banks of Issue.

ESMA's Assessment of UK-based CCPs under Article 25(2c) of EMIR

ESMA's assessment was conducted in accordance with the [Methodology for assessing a Third Country CCP under Article 25\(2c\) of EMIR](#), which was published on ESMA's website in July 2021.

ESMA identified several scenarios in which the two Tier 2 CCPs established in the UK may potentially pose a financial stability risk to the EU or individual Member States, through the provision of certain clearing services to EU entities and markets in certain EU currency denominated products.

In particular, the assessment identified three clearing services as being of substantial systemic importance to the EU or to one or more of its Member States. These are SwapClear of LCH Ltd for the clearing of interest rate derivatives denominated in euro and Polish zloty, as well as the Credit Default Swaps service (CDS) and the Short-Term Interest Rate Derivatives service (STIR) of ICE Clear Europe Ltd, in both cases for euro-denominated products.

Based on a comprehensive analysis of costs, benefits, and consequences, the assessment concluded that at this point in time the costs of derecognising these clearing services would outweigh the benefits. Therefore, under the current circumstances, ESMA is not recommending to the European Commission that the Tier 2 CCPs should not be recognised under EMIR to provide these substantially systemic important services to clearing members and trading venues established in the EU.

Proposed risk mitigation measures

The assessment nonetheless identified important risks and vulnerabilities in connection with a continued recognition of these clearing services, in particular, in times of distress, taking into account the size of the exposures of EU clearing members and clients, interconnections between the clearing services and the EU, and a lack of alternative clearing services.

All three clearing services have dominant market shares in one or more EU currency denominated products, creating dependencies of EU market participants, including banks, non-bank financial entities, and non-financial entities. Given the high credit and liquidity exposures of EU clearing members, under certain scenarios this may create financial stability risks for the EU, individual Member States, or EU currency areas.

Furthermore, insufficient supervisory powers, particularly in crisis events and including in the context of a Tier 2 CCP recovery or resolution, may hamper EU authorities' access to timely information and the possibility to intervene effectively to manage financial stability risks for the EU or individual Member States.

Therefore, ESMA is of the opinion that appropriate measures to reduce and mitigate such risks should be considered by the relevant EU institutions and authorities. ESMA is also suggesting a review of the effectiveness of these measures after an appropriate period of their implementation. Specifically, ESMA suggests the following steps be taken:

Appropriate incentives to reduce exposures to Tier 2 CCPs

Consideration should be given to measures of regulatory and/or supervisory nature that would incentivise EU clearing participants and EU clients to reduce their exposures towards Tier 2 CCPs and to rebalance these towards EU CCPs, with a view to reducing their substantial systemic importance for the EU and so the identified risks. Measures to be considered by the relevant EU institutions and authorities could include requirements for alternative clearing arrangements for clearing members or clients, and appropriate prudential requirements to effectively incentivise the participants to reduce their exposures to the Tier 2 CCPs. The relevant EU authorities should also consider the implications that such regulatory and supervisory incentives may have, including on the potential direction of the migration of clearing services from Tier 2 CCPs to EU CCPs.

Revision of the framework for comparable compliance

The framework for comparable compliance should be reviewed with a view to providing ESMA with appropriate tools to fully assess ongoing compliance with EMIR. In particular, it should provide ESMA with the flexibility to take the degree of systemic importance of the Tier 2 CCP being assessed into account. It should also make explicit that the granting of comparable compliance to a Tier 2 CCP does not limit or void ESMA's supervisory and enforcement powers over the Tier 2 CCP for the EMIR-requirements for which the Tier 2 CCP has been deemed comparably compliant. Especially in the case of urgent need or where there would be vastly different supervisory outcomes under the EU and third-country regimes, ESMA should still be competent to take action.

Expansion of ESMA's supervisory and crisis management toolbox

ESMA's powers should be reviewed and extended so that risks related to a crisis situation, including in a recovery and resolution scenario, can be better mitigated. In particular, the establishment of a clear and comprehensive toolbox for times of distress could bolster the preparedness of CCPs and could be conceived in such a way to ensure a greater involvement of ESMA to prepare for the potential recovery and resolution of a Tier 2 CCP and so, to deal with the fallout of the declining health of such Tier 2 CCP in a better and more coordinated way. In particular, this should entail the following:

1. Appropriate tools should be introduced to address the cross-border systemic risks during a crisis, including in a recovery and resolution situation, of Tier 2 CCPs accessed

by clearing participants established in the EU. At present, ESMA has no ex-ante powers to mitigate such risks since neither EMIR nor the CCP Recovery and Resolution Regulation (CCPRRR) include any specific ESMA role vis-à-vis Tier 2 CCPs.

2. The extent to which Tier 2 CCPs can be required to comply directly with all or part of the provisions embedded in the CCPRRR should be examined, with gaps addressed accordingly. Currently, a Tier 2 CCP must comply with Article 16, Title IV, and Title V of EMIR to qualify to be recognised. However, there is no corresponding obligation in respect of CCPRRR requirements.
3. ESMA should be granted with an approval power in respect of the recovery plans for Tier 2 CCPs, in order to evaluate whether there is a need to limit potential negative impacts on EU market participants and EU financial stability.
4. ESMA should be consulted by relevant third country authorities before the validation of the resolution plan of a Tier 2 CCP. Moreover, in the case of the resolution of a Tier 2 CCP, ESMA should be consulted before any discretionary measures are taken that could potentially have adverse impacts on an EU market participant and, potentially, on EU financial stability (such as a decision to terminate access of an EU bank to a third country CCP that is under resolution).
5. ESMA should be granted the power to request to be consulted by Tier 2 CCPs and third country resolution authorities prior to their imposing any restriction, suspension, or termination of access to EU clearing members. This would supplement the above proposed consultation powers for recovery and resolution events.

Enhancement of cooperation with UK authorities on CCP recovery and resolution

Finally, a new mandate should be included in the CCPRRR to provide ESMA with the possibility to negotiate a recovery and resolution specific MoU with the relevant authorities on Tier 2 CCPs.

Notes for editors

1. ESMA's mission is to enhance investor protection and promote stable and orderly financial markets. It achieves these objectives through four activities:
 - i. assessing risks to investors, markets and financial stability;
 - ii. completing a single rulebook for EU financial markets;
 - iii. promoting supervisory convergence; and
 - iv. directly supervising specific financial entities.
2. The review of the European Markets Infrastructure Regulation (EMIR, Regulation EU (No) 648/2012)), or EMIR 2.2., enhanced the role of ESMA. ESMA received direct supervisory responsibilities for systemically important third country CCPs. Both LCH Ltd and ICE Clear Europe Ltd have been recognised by ESMA as systemically important third country CCPs (so-called Tier 2), based on pre-defined criteria, and following the equivalence decision of the European Commission on the regulatory and supervisory framework of the UK for CCPs. The objective of the increased role for ESMA is to ensure an adequate monitoring and management of the risk that Tier 2 CCPs may pose to the EU.
3. For EU CCPs, ESMA's responsibilities also increased to enhance supervisory convergence and ensure a resilient CCP landscape. For example, ESMA will provide opinions on draft decisions by a national competent authority concerning the compliance of an EU CCP with certain requirements of EMIR. Other tasks of ESMA relate to, for example, the ESMA CCP stress test and peer reviews.
4. A distinct committee has been set up within ESMA, which is the CCP Supervisory Committee. The CCP Supervisory Committee is composed of a Chair, two Independent Members and representatives of the national competent authorities with an authorised CCP as voting members, as well as central banks of issue that have requested membership to the Committee as non-voting members. In addition to being responsible for a number of tasks in relation to CCPs established in the EU, the Committee is responsible for certain tasks in relation to CCPs established in third countries, with the objective to ensure an adequate monitoring and management of the risk they may pose to the EU. This relates, in particular, to the preparation of decisions regarding the recognition of TC CCPs and the supervision of Tier 2 CCPs, including the tiering and comparable compliance assessments as well as the review of recognitions.

5. Article 25(2c) EMIR provides that ESMA may, on the basis of a fully reasoned assessment, conclude that a CCP or some of its clearing services are of such substantial systemic importance that that CCP should not be recognised to provide certain clearing services. Substantial systemic importance entails that the respective CCP services are assessed to have the potential to negatively impact EU financial stability, even though they are in full compliance with EMIR. After the issuance of a recommendation by ESMA, the Commission may, as a measure of last resort, adopt an implementing act specifying that some or all of the clearing services of the involved CCP can only be provided to clearing members and trading venues established in the EU after the CCP has obtained authorisation under EMIR.
6. ESMA can recognise Tier 2 CCPs only if they are compliant with Article 16 (capital requirements), Title IV (requirements for CCPs, including organisational, conduct of business, and prudential requirements), and Title V (requirements on interoperability arrangements) EMIR. In contrast, the mechanism of comparable compliance entrenched in Article 25a EMIR enables these CCPs to be deemed compliant with these provisions through compliance with the comparable requirements applicable in the relevant third country.