



BANK OF ENGLAND

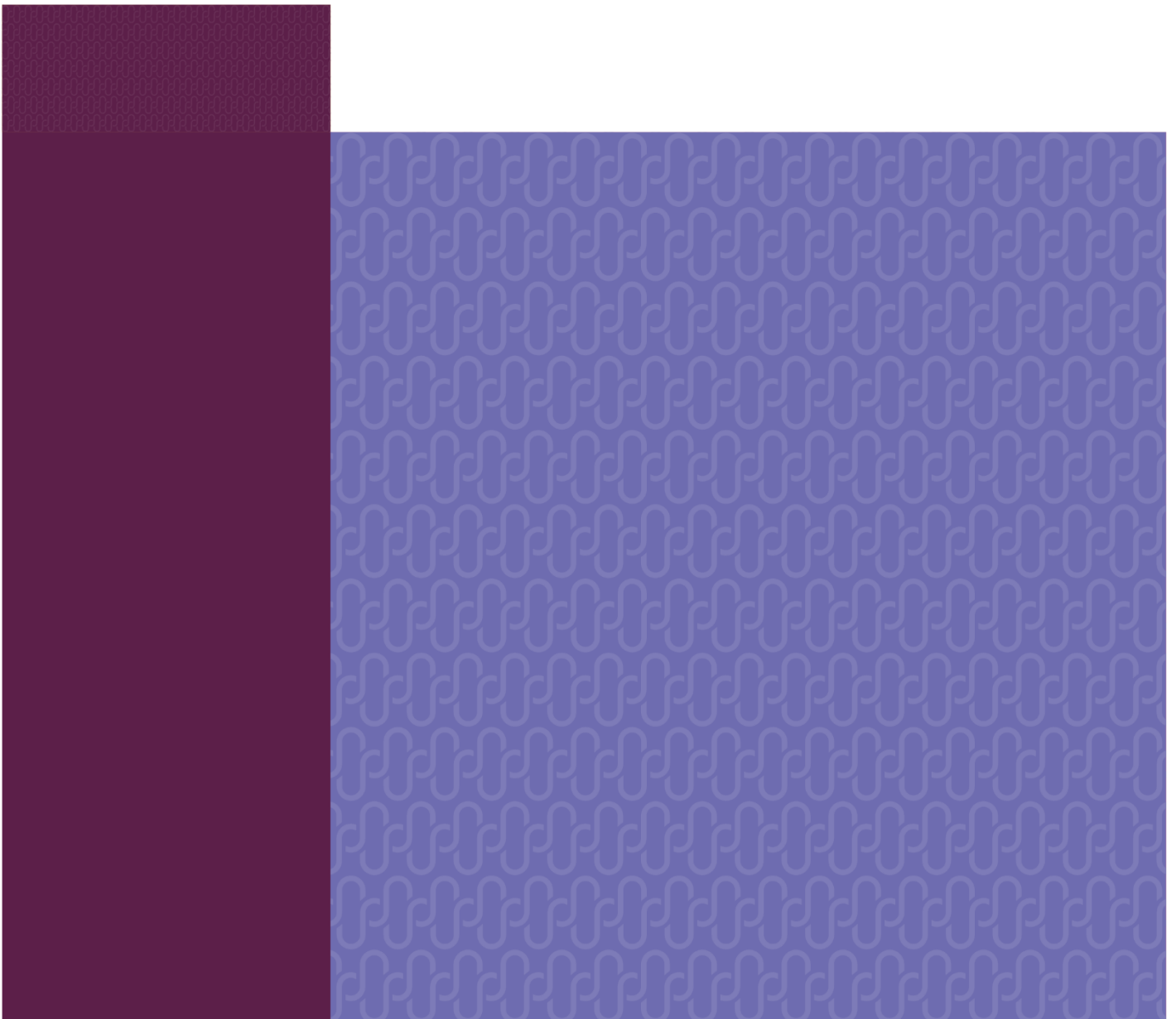
Financial Market
Infrastructure



Statement of Policy

The Bank of England's approach to tiering incoming central counterparties under EMIR Article 25

June 2022



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1 Introduction

1.1 This Statement of Policy (SoP) is relevant to incoming central counterparties (CCPs) that are seeking recognition by the Bank to provide services in the UK,¹ and relevant home authorities.

1.2 Under the on-shored European Market Infrastructure Regulation (EMIR),² the Bank is required to 'tier' incoming CCPs based on the degree to which the CCP poses, or is likely to pose, risks to UK financial stability. An incoming CCP that is designated Tier 2 (where that CCP is systemically important or likely to become systemically important for the financial stability of the UK) will become subject to direct UK supervision and regulation. An incoming CCP that is designated Tier 1 will be primarily supervised and regulated by its home authority.

1.3 This SoP sets out the Bank's approach to tiering incoming CCPs according to the level of systemic risk they potentially pose to UK financial stability as well as providing a guide to the type of information the Bank will consider in making its tiering designations.

Implementation

1.4 The Bank will implement its approach to tiering incoming CCPs from Thursday 1 December 2022.

¹ Including those currently in the Temporary Recognition Regime. For the full list see [List of third-country CCPs that are taken to be eligible for temporary deemed recognition in the UK by virtue of the Temporary Recognition Regime established by the Central Counterparties \(Amendments, etc., and Transitional Provision\) \(EU Exit\) Regulations 2018 as amended](#).

² See in particular Article 25 of Regulation (EU) 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories as it forms part of retained EU law, and in particular as amended by the Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2020. Unless otherwise stated, any references to EU or EU-derived legislation refer to the version of the legislation which forms part of retained EU law.

2 Definitions

Default fund contribution

2.1 A default fund contribution (DFC) is a pool of funds established by a CCP, comprising pre-funded financial contributions provided by clearing members, to mutualise any losses arising in the event that one or more participants defaults on their obligations to the CCP and resources provided by the defaulting party (or parties) are not sufficient to cover such losses.

Incoming CCP

2.2 A non-UK CCP that is seeking recognition by the Bank to provide clearing services to clearing members or trading venues established in the UK.

Informed reliance assessment

2.3 An informed reliance assessment is the process whereby the Bank determines the extent to which the Bank is able to rely on the incoming CCP's home authority for supervision and regulation of that CCP.

Initial margin

2.4 Initial margin (IM) is collateral that is posted by a CCP's clearing members to protect the transacting parties from the potential future exposure that could arise from future changes in the mark-to-market value of the contract during the time it takes to close out and replace the position in the event that one or more counterparties default. When used in this SoP, the term IM includes margin add-ons and IM posted by clearing members on behalf of clients (regardless of the jurisdiction of those clients).

Interoperability

2.5 An arrangement between two or more CCPs that involves a cross-system execution of transactions. Interoperability allows participants in different CCPs to clear and settle financial transactions across CCPs without participating in multiple systems.

Relevant home authorities

2.6 Any relevant national or international authority which may, in the Bank's judgement, have a significant impact on:

- the regulatory or supervisory framework applicable to the incoming CCP; and/or
- the supervisory outcomes in relation to the incoming CCP.

Tiering

2.7 Tiering is the classification of individual incoming CCPs based on the degree to which the CCP poses, or is likely to pose, risks to UK financial stability. An incoming CCP that is designated Tier 2 (where that CCP is systemically important or likely to become systemically important for the financial stability of the UK) will become subject to direct UK supervision and regulation. An incoming CCP that is designated Tier 1 will be primarily supervised and regulated by its home authority.

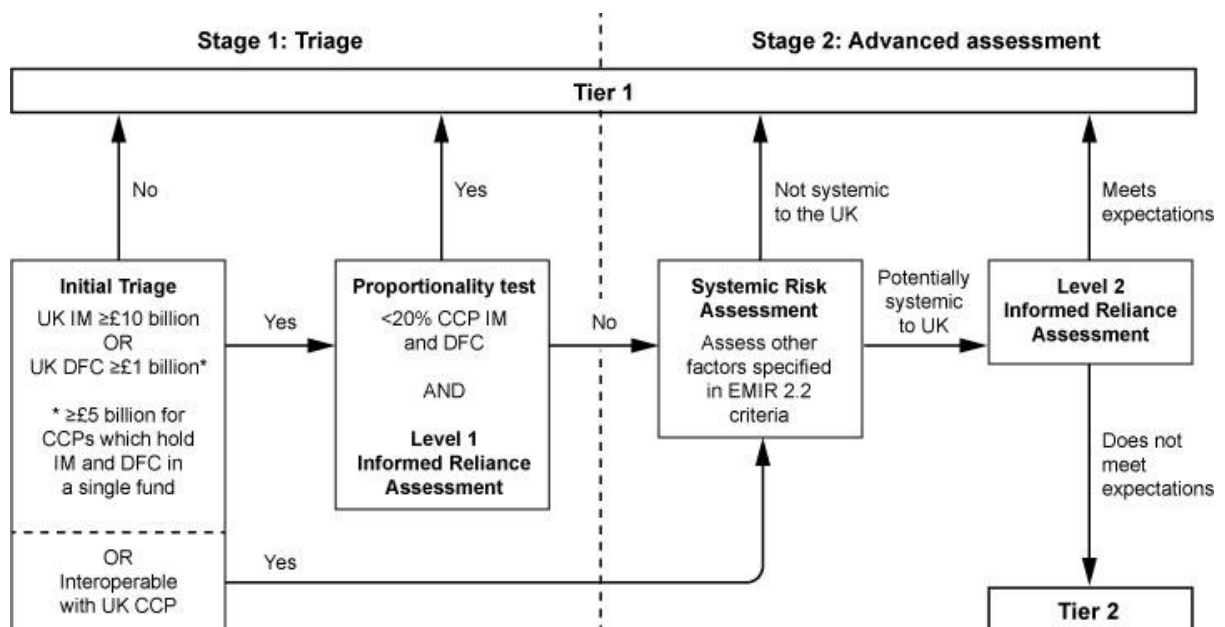
3 The Bank’s approach to tiering incoming CCPs

3.1 The Bank will undertake a two-stage process to assess whether an incoming CCP should ultimately be designated as a Tier 1 or Tier 2 CCP. The process is consistent with the statutory framework for the Bank to determine whether an incoming CCP is systemically important or likely to become systemically important for the financial stability of the UK in accordance with EMIR Article 25(2a).

3.2 The Bank will review information directly submitted from incoming CCPs and relevant home authorities as required, in order to aid its decision-making process.

3.3 The diagram below provides a summary of the Bank’s approach to tiering incoming CCPs.

Figure 1: Summary of the Bank’s approach to tiering of incoming CCPs



Stage 1: Triage

3.4 The Bank will assess the following indicators to initially ‘triage’ incoming CCPs when they apply for recognition to provide clearing services to clearing members and trading venues established in the UK:

- **Initial margin**: whether the incoming CCP has held at least £10 billion of UK clearing member IM (pre-haircut, including IM from non-UK subsidiaries of UK headquartered firms) across all services, at any point in the last five calendar years prior to the submission of the recognition application. This IM figure is inclusive of any margin add-ons and inclusive of IM clearing members post on behalf of clients.

- **Default fund contributions:** whether the incoming CCP has held at least £1 billion³ of UK clearing member DFCs (including DFCs from non-UK subsidiaries of UK headquartered firms) across all services at any point in the last five calendar years prior to the submission of the recognition application.
- **Interoperability:** whether the incoming CCP has an interoperability arrangement in place with a UK CCP.

3.5 An incoming CCP that does not meet any of these criteria will usually not move forward to the next stage of the tiering assessment and will be classified as a Tier 1 CCP. An incoming CCP that meets one or more of these criteria will move forward to the next steps of the process.

3.6 The Bank may apply judgment in applying the triage criteria outlined in paragraph 3.4. For example, if the incoming CCP is close to one or more of the triage indicators (above or below), or the incoming CCP's IM and DFC metrics are trending up or down, the Bank may use its judgement to opt whether or not to further assess the incoming CCP before making a tiering determination.

3.7 For those incoming CCPs that meet one or both of the first two triage criteria (ie IM or DFC), but not the interoperability criterion, the Bank will conduct a test to assess the proportion of total i) IM and ii) DFC attributable to UK clearing members (including non-UK subsidiaries of UK headquartered firms) (the 'proportionality test'). In other words, this test will broadly assess the proportion of UK clearing member activity to the total of all clearing activity at a particular incoming CCP. The Bank has set the proportionality thresholds at 20% of the incoming CCP's total IM and DFC from all CMs. This will be calculated based on a five-year average of IM and DFC across all services at the incoming CCP.

3.8 Where both the IM and DFC attributable to UK clearing members (or subsidiaries of UK headquartered clearing members) are below 20%, the Bank will determine if the Bank is able to place reliance on the incoming CCP's home authority's regulation and supervision via a Level 1 informed reliance assessment. The Level 1 informed reliance assessment may be conducted during the tiering process, or, in certain circumstances, may have been conducted in advance at the request of home authorities (as set out in 3.14).

3.9 An incoming CCP that is below the proportionality test thresholds and where the Bank's expectations for the Level 1 informed reliance assessment have been met, will be classified as Tier 1.

3.10 Where either or both the IM and DFC attributable to UK clearing members (or subsidiaries of UK headquartered clearing members) is at or above 20%, or where the Level 1 informed reliance assessment expectations have not been met by the relevant home authority, the incoming CCP will move to Stage 2 of the tiering process.

3.11 An incoming CCP that meets the interoperability triage criterion will move forward to Stage 2 of the process and will not be subject to the proportionality test and the Level 1 informed reliance assessment.

³ Or £5 billion for CCPs which hold IM and DFC in a single fund.

Contents of the Level 1 informed reliance assessment

3.12 For those incoming CCPs that are below the proportionality test thresholds, the Bank will consider the following as part of the Level 1 informed reliance assessment:

- The regulatory framework in the home jurisdiction in so far as it applies to the incoming CCP.
- The nature, extent and degree of supervision of the incoming CCP as conducted by the home authority.
- The Bank's relationship with all relevant home authorities, including, where appropriate, co-operation arrangements and transparency around the regulation and supervision of the incoming CCP.

3.13 The Bank will also take relevant home authorities' regulatory and supervisory priorities into consideration, including whether authorities responsible for regulating and supervising globally systemic CCPs act in the interests of protecting financial stability. Where the Bank has an existing relationship with the relevant home authorities, the Bank will consider the effectiveness of the co-operation arrangements it already has in place with those authorities and whether any changes would be necessary.

3.14 Home authorities with which relevant co-operation arrangements exist between the Bank and the authority (eg a CCP-specific MoU has been agreed between the Bank and the home authority since the EMIR 2.2 framework was adopted (ie via Regulation (EU) 2019/2099) on 23 October 2019) may request a Level 1 informed reliance assessment prior to the tiering process. Where the quality of supervision by the home authority is found to meet the Level 1 criteria in relation to the incoming CCP, the result of the early assessment could be used by the Bank with respect to the relevant incoming CCPs to satisfy the requirements of Level 1 informed reliance within the tiering process (ie as set out in 3.8).

3.15 For home regulatory and supervisory authorities which have little or no previous bilateral relationships with the Bank, an informed reliance assessment will consider whether, in the judgement of the Bank, an effective co-operative relationship is likely to develop with the relevant home authorities. This will be determined on the basis of the key factors outlined in the table in Annex 1.

3.16 To the extent possible, the Bank will rely on information submitted as part of the equivalence process.⁴

3.17 The key areas the Bank will review when assessing the extent to which the Bank is able to rely on the relevant home authorities are outlined in the table in Annex 1. The items in this table are non-exhaustive and the Bank may take other relevant considerations into account for the purposes of the assessment. In order to aid its review, the Bank may also request information and/or clarifications from the relevant home authorities.

⁴ Under EMIR Article 25(6) HM Treasury is responsible for determining if the home regime is equivalent to the UK's regime; this is one of the pre-conditions for the Bank making a recognition decision in relation to an incoming CCP.

Stage 2: Advanced assessment

3.18 For those incoming CCPs that are above the proportionality test thresholds and/or for which the Level 1 informed reliance expectations have not been met, as well as for incoming CCPs meeting the interoperability criterion, the Bank will undertake a systemic risk assessment in order to assess factors relating to the incoming CCP that may impact its systemic importance to the UK and to inform a possible Level 2 informed reliance assessment (paragraph 3.23). This will include a more detailed assessment of the criteria outlined in EMIR Article 25(2a).

3.19 The indicators which the Bank deems most important for this assessment are listed in paragraph 3.21 below. The Bank will place particular emphasis on the key indicators set out below to assess systemic risk to UK financial stability, although these indicators are non-exhaustive. This assessment will also consider the diversity in a CCP's approach to margin models and default waterfalls.

3.20 If this detailed assessment indicates that an incoming CCP is not potentially systemic to UK financial stability, the incoming CCP will be designated Tier 1 (and will therefore not progress further in the tiering process).

3.21 The Bank's systemic risk assessment will include a review of all relevant information, including the following areas, to aid its tiering determinations:

- products cleared by the incoming CCP;
- margin, collateral, and default fund contributions;
- the nature of the incoming CCP's access model;
- access to alternative clearing venues; and
- interactions with other financial institutions, including interoperability arrangements.

3.22 Additional detail about the type of information the Bank will review to make its determinations is set out in Annex 2.

3.23 Where an incoming CCP is considered potentially systemic to UK financial stability according to the systemic risk assessment, the Bank will conduct a Level 2 informed reliance assessment to determine the extent to which the Bank is able to place reliance on the incoming CCP's home authority's regulation and supervision. Where the Bank's expectations for the Level 2 informed reliance assessment have been met, the incoming CCP will usually be designated Tier 1. Where the Bank's expectations have not been met, the incoming CCP will usually be designated Tier 2.

3.24 The determination of whether an incoming CCP is Tier 2 will depend on the outcome of the Level 2 informed reliance assessment along with the other factors considered in the tiering process (ie where applicable, the initial triage, proportionality test and Level 1 informed reliance assessment and systemic risk assessment). No individual assessment criterion detailed in this SoP will, in isolation, be decisive in a Tier 2 designation. The Bank's determinations will be made on the basis of a holistic assessment of all applicable criteria.

Contents of the Level 2 informed reliance assessments

3.25 For incoming CCPs that are considered potentially systemic to the UK, the Bank will consider all of the factors outlined in the Level 1 informed reliance assessment.

3.26 The key areas the Bank will review in the context of the Level 2 informed reliance assessment are outlined in the table in Annex 1. The items in the table are non-exhaustive and the Bank may take other relevant considerations into account for the purposes of the assessment. The Bank will also take into account any key factors identified during the systemic risk assessment to inform its areas of focus for the Level 2 informed reliance assessment. In order to aid its review, the Bank may also request information and/or clarifications from the relevant home authorities.

4 Reviewing Tiering Decisions

4.1 The Bank will review an existing tiering decision if there is a change which significantly impacts the incoming CCP's risk profile.

4.2 Where the Bank has reason to believe that there has been a change at the incoming CCP or the relevant home authority relative to the criteria outlined in Stage 1 or Stage 2 of the tiering assessment, the Bank will review the latest available information to decide whether the incoming CCP continues to be appropriately tiered or should be tiered differently. Incoming CCPs are obliged to notify the Bank of any material changes affecting the conditions for recognition.⁵

4.3 As set out in EMIR Article 25(5), if the Bank determines that a Tier 1 CCP should be reclassified as Tier 2, the Bank will set an appropriate adaptation period within which the incoming CCP must comply with the requirements applicable to Tier 2 CCPs.

⁵ EMIR Article 25(4b).

Annex 1: Informed reliance assessment

Area for review for the informed reliance assessment	Level 1 Informed reliance assessment	Level 2 Informed reliance assessment (in addition to the Level 1 informed reliance assessment criteria)
Regulatory co-operation		
Engagement with the relevant home authorities	<ul style="list-style-type: none"> • Does/will the Bank receive notification of relevant regulatory developments, including those that may materially affect the rules or procedures of the CCP? • Does/will the Bank consider the regulatory co-operation to be open and effective? 	<ul style="list-style-type: none"> • Does/will the Bank receive early or advance notification of new and material changes to regulations affecting the CCP?
Supervisory co-operation		
Engagement with the relevant home authorities	<ul style="list-style-type: none"> • Does/will the Bank participate in appropriate bilateral or multi-lateral fora with the relevant home authorities to discuss supervisory issues relating to the CCP at least annually? This could include one or more of the following: <ul style="list-style-type: none"> ○ Bi-lateral meetings at principal and working level. ○ Participation in supervisory colleges, where applicable. • Does/will the Bank consider the supervisory co-operation to be open and effective? 	<ul style="list-style-type: none"> • Does/will the Bank have an agreed multi-layer engagement strategy that includes updates and exchange of views on key risks and priorities at least quarterly? This could be achieved by the following: <ul style="list-style-type: none"> ○ Bi-lateral meetings at principal and working level. ○ Participation in supervisory colleges, where applicable. ○ For interoperable CCPs, participation in interoperable roundtable. ○ The Bank being invited to join a supervisory visit, to join a supervisory examination or participate in a model review (at least one of these annually).
Supervisory aims and priorities	<ul style="list-style-type: none"> • Does/will the Bank have a sound understanding of the relevant home authorities' supervisory approach and priorities as they apply to the CCP? 	<ul style="list-style-type: none"> • To what extent do/will the relevant home authorities' supervisory priorities for the CCP align with the Bank's priorities? • Does/will the Bank have confidence that the relevant home authorities will include

		the Bank’s views as a source of input ⁶ into its decision-making when setting its priorities?
Information sharing		
	<ul style="list-style-type: none"> • Do/will the relevant home authorities share relevant information regarding the CCP with the Bank in a timely manner? • Does/will the information shared enable the Bank to assess that supervisory outcomes are broadly similar to those of the Bank on an ongoing basis? This might include sharing of priorities and the supervisory work plan and high-level summaries of decisions on key matters (eg model changes, extension of services etc). • Do/will the relevant home authorities notify the Bank promptly of material events to the CCP? 	<ul style="list-style-type: none"> • More detailed information sharing. This might include (but is not limited to): <ul style="list-style-type: none"> ○ Summaries of risk reviews, model reviews, significant supervisory reviews. ○ Review and assessment letters sent from the relevant home authorities to the CCP. ○ Review of the CCP’s self-assessment against PFMIs. ○ Periodic information sharing on areas of common interest and horizon scanning.
Crisis management		
	<ul style="list-style-type: none"> • Where applicable, have/will the relevant home authorities shared/share enough relevant information about the CCP with the Bank in a timely manner during crises? • If not, does/will the Bank have confidence that the relevant home authorities would share timely, relevant information? 	<ul style="list-style-type: none"> • Does/will the Bank participate in a crisis management group (or equivalent) operated by the home jurisdiction, where the CCP is discussed? • If not, does/will the Bank have confidence that it will be invited to participate in the crisis management group?

⁶ This should not undermine the primacy of the relevant home authority and should be proportionate.

Other considerations	
Dispute resolution	Does/will the Bank have acceptable dispute resolution procedures with the relevant home authorities?
Engagement with international standards	The extent to which the home jurisdiction has engaged/will engage with, and has committed/will commit to, international regulatory fora, such as the Committee for Payments and Market Infrastructure (CPMI) or International Organization of Securities Commissions (IOSCO).
Regulatory environment	Overall assessment of co-operative nature of relevant home authorities, including the extent to which the relevant home authorities have/will have policies in place that may influence the likelihood of the CCP becoming systemically important to the UK.

Annex 2: Systemic risk assessment

EMIR Art 25(2a) criteria	Bank review area	Information the Bank will review
The nature, size and complexity of the CCP's business in the UK, and outside the UK to the extent its business may have a systemic impact on the UK (EMIR Article 25(2a)(a)).	<ul style="list-style-type: none"> • Products cleared by the incoming CCP. 	<ul style="list-style-type: none"> • Sterling and non-sterling products cleared by the incoming CCP, including information about the volumes cleared, liquidity and underlying reference, and the currency of denomination.
The effect that the failure of or a disruption to the CCP would have on financial markets, including the liquidity of the markets served, financial institutions, the broader financial system or the financial stability of the UK (EMIR Article 25(2a)(b)).	<ul style="list-style-type: none"> • Margin, collateral, and default fund contributions. 	<ul style="list-style-type: none"> • The total DFC held by the incoming CCP, by currency. • The DFC made to the incoming CCP by UK clearing members (including overseas subsidiaries of UK headquartered firms), by currency. • The total IM held by the incoming CCP by underlying asset, currency, and split between house and client accounts. • The total IM and DFC attributable to UK clearing members (including non-UK subsidiaries of UK headquartered firms) by underlying asset, currency, and split between house and client accounts. • The total value of cash and non-cash collateral.
The CCP's clearing membership structure including, to the extent the information is available, the structure of its clearing members' network of clients and indirect clients, established in the UK (EMIR Article 25(2a)(c)).	<ul style="list-style-type: none"> • The nature of the incoming CCP's access model. 	<ul style="list-style-type: none"> • Access model and membership requirements. • The extent to which UK clients access the incoming CCP via UK clearing members (including non-UK subsidiaries of UK headquartered firms) and non-UK clearing members.

<p>The extent to which alternative clearing services provided by other CCPs exist for clearing members and, to the extent the information is available, their clients and indirect clients established in the UK (EMIR Article 25(2a)(d)).</p>	<ul style="list-style-type: none"> • Access to alternative clearing venues. 	<ul style="list-style-type: none"> • The availability of alternative clearing venues to those offered by the incoming CCP, and the ability of UK clearing members and UK clients to access those alternative venues. • Whether the products offered are subject to the mandatory clearing obligation.
<p>The CCP's relationships, interdependencies, or other interactions with other financial market infrastructures, other financial institutions and the broader financial system to the extent that that is likely to have an impact on the financial stability of the UK (EMIR Article 25(2a)(e)).</p>	<ul style="list-style-type: none"> • Outsourcing and third-party service providers. • Interoperability with UK CCPs. 	<ul style="list-style-type: none"> • A list of critical service providers and the services they are responsible for delivering. • A detailed description of the interoperability arrangement (IA), including the value of transactions cleared via the IA, the margin collected/posted via the IA and the settlement payment obligations arising from the interoperable link.