BANK OF ENGLAND

Financial Market Infrastructure

Consultation Paper

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

November 2021

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Responses are requested by Friday 25 February 2022.

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1 Overview

1.1 Following the UK's withdrawal from the European Union ('EU'), the Bank of England ('the Bank') has responsibility for recognising and supervising non-UK central counterparties ('incoming CCPs') intending to provide clearing services to clearing members or trading venues established in the UK.

1.2 This Consultation Paper ('CP') and draft Statement of Policy ('SoP') set out the Bank's proposed approach to 'tiering' incoming CCPs. Tiering is the classification of individual incoming CCPs according to the level of systemic risk they could pose to UK financial stability. CCPs that are not considered systemically important to the UK or likely to become systemically important will be designated 'Tier 1' CCPs. If incoming CCPs are considered to pose risks to UK financial stability, the Bank can potentially designate them as 'Tier 2' CCPs, which results in those CCPs becoming subject to direct UK supervision and regulation under the on-shored European Market Infrastructure Regulation (EMIR[1]). Under EMIR, the Bank may also recommend to HM Treasury that it make location regulations if the Bank considers that an incoming CCP is of such substantial systemic importance to the UK that it should not be recognised (known as 'location regulations' and sometimes referred to as 'Tier 3').

1.3 This CP is relevant to incoming CCPs that are seeking recognition by the Bank to provide services in the UK (including those currently in the Temporary Recognition Regime[2]), and relevant national authorities.

1.4 Following the UK's withdrawal from the EU, the UK has retained the EU framework for recognising incoming CCPs (known as 'EMIR 2.2'). The legal framework allowing an incoming CCP to provide clearing services to clearing members or trading venues established in the UK is set out in EMIR Article 25 and at a high level involves three key steps:

- Equivalence[3]: a determination by HM Treasury that the home-country regime is equivalent to the UK's regime;
- Cooperation arrangements[4]: established with the relevant national authority;
- Recognition[5]: authorisation by the Bank of individual CCPs to provide clearing services to clearing members or trading venues established in the UK. Tiering decisions form part of the recognition process under EMIR.

1.5 The Bank is responsible for finalising policy on important areas of the implementation of EMIR 2.2 in the UK. This CP sets out the Bank's proposed approach to tiering as part of the 'recognition' step described above. The Bank is concurrently consulting on its approach to assessing comparable compliance (and in due course the Bank will also consult on its approach to setting fees for incoming CCPs).

1 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 For the full list see here.
3 EMIR Article 25(6)
4 EMIR Article 27(7) and EMIR Article 25(2)(c)
5 EMIR Article 25(1)

2 Background

What are CCPs?

2.1 Financial market infrastructures (FMIs) such as CCPs lie at the heart of the financial system, providing crucial functions that help the economy and financial markets operate.

2.2 CCPs improve the efficiency and stability of financial markets by placing themselves in the middle of trades between buyers and sellers and guaranteeing their performance to each other on certain transactions. CCPs therefore play an important role in reducing counterparty credit risk in the financial system. This is the risk that one party to a financial market trade defaults on its obligations to the counterparty on the other side of that same trade. Without a CCP, the default of a party on either side of a trade could result in financial distress for both parties. This could have potential knock-on effects on their other trades and counterparties, and even the rest of the financial system. When a trade is cleared through a CCP, that CCP can act as a 'shock absorber' in the event of a default, reducing the risk of contagion through financial markets.

2.3 CCPs reduce counterparty credit risk in two main ways. First, CCPs have arrangements in place to manage the counterparty risk of their clearing members in an orderly way. For example, CCPs hold large amounts of margin collateral from their counterparties (margin), and have other resources, rules and arrangements to manage exposures in the event of a clearing member default. These resources usually consist of the mutualised loss absorbing capacity of the default funds to which all clearing members contribute, some of the CCPs' own capital (their 'skin in the game') and other loss allocation arrangements.

2.4 Second, CCPs enable the reduction of exposures in the financial system. CCPs can offset amounts owed between their clearing members through a process known as multilateral netting. This also reduces the total collateral and liquidity needs of CCP clearing members. This is because market participants replace their exposure to multiple counterparties with a single exposure to the CCP.

2.5 In the years following the global financial crisis of 2007–08, the G20 introduced global financial market reforms, which were designed to increase the use of central clearing. These reforms enhanced financial stability by simplifying the network of counterparty exposures between financial institutions, and reducing the aggregate size of these exposures. However, in achieving this objective, CCPs have become increasingly interconnected with their clearing members, liquidity providers, custodians and other financial institutions.

Why are CCPs important to financial stability?

2.6 CCPs now sit at the heart of a very wide range of domestic and global financial transactions – helping to ensure that, unlike in 2008, the default of a single counterparty does not lead to contagion and panic. As a result, CCPs have also become increasingly important to financial stability. Actions taken by CCPs during their normal course of business, during market stress, or in the event of a clearing member default, all have the potential to have significant impacts on other parts of the financial system and market participants.

2.7 For example, CCP margin requests are critical to reduce and mitigate counterparty credit risk in the financial system. This reduction in counterparty credit risk is a major accomplishment of the post 2007-08 reforms. However, requests for margin also create liquidity demands on clearing members and clients and could, if abrupt or large, be destabilising during periods of market stress.

2.8 In the event of the clearing member default(s), non-defaulting clearing members' resources in a CCP's default fund are at risk of depletion. CCPs might also be forced to request additional resources from non-defaulting clearing members if their initial contributions to the default fund are depleted. Likewise, without sufficient liquid resources, or where a liquidity provider fails, a CCP's ability to meet its obligations to clearing members might be impeded.

2.9 Due to this increased importance of CCPs, international regulators have sought to strengthen CCP resilience to support financial stability. There has also been increased focus on the importance of regulating and supervising cross-border CCPs in a manner that is consistent and in line with global standards. This CP includes proposals that aim to further this objective with respect to those CCPs that offer services in multiple jurisdictions but are not incorporated in the UK.

The Bank's high-level approach to incoming CCPs

2.10 Following the UK's withdrawal from the EU and the end of the transition period, the Bank was given new powers to determine which incoming CCPs are able to provide services in the UK. This section sets out the Bank's overall approach that underpins our use of these new powers.

2.11 Wholesale market infrastructure often operate across borders. This is a desirable feature, which allows them to provide a seamless network of functions that comes with significant financial stability benefits. These include deeper pools of liquidity; reduced concentration risk; and reduced fragmentation in regulation and supervision – all contributing to a reduction of systemic risk on a global scale, and also reducing the cost to users as the number of users grow.

2.12 Central clearing has grown significantly over the past decade – about 60% of credit default swaps are cleared, as well as 80% of interest rate contracts, up from about 10% and 40% respectively in 2008.[6] Central clearing is done across borders and currencies: the operations behind a routine financial transaction – issuing corporate debt, adjusting a pension fund portfolio or hedging against the risks of commodity price increases – will typically involve a wide range of financial firms over many jurisdictions. The growth of global infrastructure that spans national borders is therefore a direct and desirable result of the reforms that were put in place after 2008.

2.13 However, while the cross-border nature of clearing can contribute to financial stability, it can also mean that risks can be imported across borders. This is particularly the case for a global centre for financial services such as the UK; many institutions based here access clearing services from central counterparties across the world.

2.14 For clearing markets to operate efficiently and these risks to be appropriately mitigated, there must be a consistent approach for the regulation and supervision of cross-border CCPs. The Principles for Financial Market Infrastructure, issued in 2012, provide an internationally agreed foundation.

2.15 Effective supervisory co-operation, including some degree of deference to other authorities, is also necessary to help ensure that internationally active CCPs are subject to clear, certain and coordinated regulatory requirements and actions that do not conflict or overlap – a critical feature in

6 Bank of International Settlements Statistical Release, November 2020.

times of extreme market stress and necessary for financial stability. However, this must be done in a safe way, to ensure risks are appropriately managed.

2.16 Such a commitment to regulatory deference was agreed in the 2013 G20 declaration, which emphasizes the importance of regulators deferring to one another when justified by the quality of the regulatory and enforcement regimes.[7]

2.17 The Bank's approach to incoming CCPs is built upon this principle of deference to other regulator's regimes - where justified - and a proportionate but diligent approach to overseeing the risk channelled from overseas CCPs. This allows the market to maximise the benefits from access to cross-border clearing while ensuring the risks are appropriately managed.

Applying these principles to the Bank's tiering approach

2.18 This CP sets out key practical aspects of how the Bank intends to implement this approach when 'tiering' incoming CCPs. As part of this, the Bank has discretion – within the parameters set out in the relevant legislation – to determine what degree of direct regulation and supervision by the Bank an incoming CCP should be subject to through the process of 'tiering'.

2.19 Under the Bank's proposed tiering approach, the Bank will seek to rely on to regulation and supervision by the home authority wherever we consider it appropriate, proportionate and safe to do so. In order to place reliance on home supervision, the Bank will need to have appropriate cooperation and information sharing arrangements in place in order to gain sufficient assurance that the home authority's regime is delivering equivalent outcomes to Bank supervision which meet the Bank's statutory financial stability objective to protect and enhance UK financial stability. The Bank does not envisage at present recommending the use of location regulations or 'Tier 3' as part of this framework.

2.20 The Bank's proposed approach is also risk-based, such that the potential risk an incoming CCP poses to the UK will determine the degree of supervisory and regulatory cooperation and information sharing we would require in order to rely on the home authority.

2.21 In developing its approach, the Bank has endeavoured to apply standards that would be practicable if applied globally. This includes recognising that the authorities with the greatest interest in a CCP, should have commensurate input in their regulation and supervision.

2.22 There are circumstances where more direct regulation and supervision by the Bank may be appropriate. Even where this is the case, the Bank will respect the primacy of the home authority and recognise that it would typically lead the regulatory response to a crisis. The Bank will not expect the home authority to act in a way that is inconsistent with its mandate. It will also take into account the interests of other authorities where they also have responsibilities in managing risks associated with incoming CCPs.

Tiering categories and recognition requirements under EMIR

2.23 The current legal framework allowing an incoming CCP to provide clearing services to clearing members or trading venues established in the UK is set out in EMIR Article 25. Under this

7 G20 Leaders' Declaration, St. Petersburg Declaration, 6 September 2013.

framework, the Bank must 'tier' incoming CCPs according to the level of systemic risk they could pose to UK financial stability.

2.24 **Tier 1**: A CCP that has not been determined as systemically important or likely to become systemically important will be designated a 'Tier 1' CCP. Before the Bank may recognise an incoming Tier 1 CCP, such CCPs are required to meet recognition requirements in EMIR Article 25(2). These requirements include i) HM Treasury making a determination that the home authority's legal and supervisory frameworks are equivalent to UK requirements and subject to effective supervision and enforcement[8] ; and ii) the Bank establishing effective cooperation arrangements with relevant authorities meeting the minimum specifications set out in Article 25(7) of EMIR.

2.25 **Tier 2:** A CCP that has been determined, in accordance to the criteria set out in this CP, to be systemically important or likely to become systemically important in the UK will be designated a 'Tier 2' CCP. Notably in assessing systemic importance the Bank will consider the potential risks the CCP could pose, taking into account the quality, effectiveness and depth of the Bank's cooperation with its home authorities. In addition to meeting the recognition requirements for Tier 1 CCPs, Tier 2 CCPs will also be required to meet certain standards set out within EMIR[9] and will be subject to direct supervision by the Bank. However, a Tier 2 CCP may request the Bank to assess whether its compliance with the regulatory requirements in its home jurisdiction satisfies the relevant EMIR standards under EMIR Article 25a ('comparable compliance'). The Bank is concurrently consulting on its approach to assessing comparable compliance in a separate Consultation Paper.

2.26 Under EMIR Article 25(2c), the Bank may also recommend to HM Treasury that it make location regulations if the Bank considers that an incoming CCP is of such substantial systemic importance to the UK that it should not be recognised. HM Treasury may then make 'location regulations' requiring that some or all of the clearing services of the CCP may only be provided to clearing members and trading venues established in the UK if they are offered from inside the UK. This is sometimes informally referred to as 'Tier 3'. Location regulations are subject to appropriate procedural safeguards and transitional provisions set out in EMIR Article 25(2c).

3 Summary of Proposals

3.1 The proposals in this CP cover:

(a) the Bank's proposed approach to assessing systemic risk potentially posed by incoming CCPs;

(b) the Bank's approach to complying with its obligations under EMIR Article 25; and

(c) the type of information the Bank may review in order to make its tiering decisions.

3.2 The Bank proposes to assess the systemic importance of incoming CCPs for the purpose of tiering in the following two stages:

8 See EMIR Article 25(6) for full details.

9 EMIR Article 16 on capital requirements, Titles IV on Requirements for CCPs and Title V on interoperability arrangements.

Stage 1: Systemic risk assessment

3.3 The Bank will undertake an initial triaging of incoming CCP to identify those that may be potentially systemic to UK financial stability. The initial triage criteria the Bank proposes to use are:

(a) **Initial Margin (IM):** Whether the incoming CCP has held at least £10bn of UK clearing member M (including non-UK subsidiaries of UK headquartered firms) across all services, at any point in the last 5 years. This IM figure is inclusive of any margin add-ons and any IM clearing members post on behalf of clients;

(b) **Default Fund Contribution (DFC)**: Whether the incoming CCP has held at least £1bn[10] of UK clearing member DFCs (including non-UK subsidiaries of UK headquartered firms) across all services at any point in the last 5 years; or

(c) **Interoperability**[11]**:** Whether the incoming CCP has an interoperability arrangement in place with a UK CCP.

3.4 The Bank proposes that an incoming CCP that does not satisfy any of these criteria will usually not need to progress to the next stage of the tiering assessment, and will be classified as a Tier 1 CCP under EMIR. Where a CCP is close to the proposed indicators the Bank may opt to further assess the CCP before making a tiering determination.

3.5 For those incoming CCPs that meet one or more of the triage criteria, the Bank proposes to undertake a more detailed systemic risk assessment in order to assess factors relating to the incoming CCP that may impact its systemic importance to the UK and ensure the triage criteria correctly identified the incoming CCP as potentially systemic for UK financial stability. This would include assessing the criteria outlined in EMIR Article 25(2a). These criteria are listed in the annex of this CP and in the draft Statement of Policy.

3.6 If this assessment indicates that the CCP is not systemically important or likely to become systemically important to the UK, the incoming CCP will be classified as Tier 1 CCP under EMIR. Otherwise the incoming CCP will progress to stage 2 of the tiering process.

Stage 2: Proportionality and Informed Reliance Assessments

3.7 In stage 2, the Bank proposes to conduct an informed reliance assessment to determine the extent to which the Bank is able to rely on home regulation and supervision of the incoming CCP.

3.8 The Bank proposes to apply two different levels of informed reliance assessment, depending on the UK interest in a CCP relative to other authorities. This is because the Bank considers that 'too many hands on the wheel' for the regulation and supervision of globally significant CCPs would be detrimental to global cross-border clearing, and is likely to increase financial stability risks via overlapping or conflicting requirements. The Bank also recognises that jurisdictions representing the highest default fund contributions to a CCP will bear the greater burden in the event of CCP failure. It is therefore appropriate that these jurisdictions should have the greatest commensurate input in their regulation and supervision.

[10] Or £5bn for CCPs which hold IM and DFC in a single fund.
[11] An interoperability arrangement is a link between central counterparties which involves the cross-system execution of transactions.

3.9 Therefore where the UK has a smaller interest in an incoming CCP relative to other jurisdictions, the Bank considers its financial stability objective is best served by relying on home authority regulation and supervision to the greatest extent possible. However, where the UK represents a significant interest in the CCP, the UK should expect a greater level of assurance that the home authority is delivering robust and equivalent supervisory outcomes.

3.10 Therefore the Bank proposes a proportionality test to assess the proportion of i) IM and ii) DFC attributable to UK clearing members (including non-UK subsidiaries of UK headquartered firms) across all services at that CCP. The Bank proposes to set these thresholds at 20% of the incoming CCP's total IM and DFC.

3.11 For incoming CCPs below these thresholds, the Bank proposes to conduct an informed reliance assessment (referred to as the 'Level 1 informed reliance assessment') to verify it has sufficient information and cooperation arrangements in place to rely on the home authority. The Bank's proposed expectations for cooperation arrangements to meet this informed reliance assessment, will be higher than those required to meet the cooperation arrangements[12] for those CCPs that are designated Tier 1 in Stage 1 of the tiering assessment.

3.12 For incoming CCPs above one or both of these thresholds, the Bank proposes to conduct a more intensive informed reliance assessment (referred to as the 'Level 2 informed reliance assessment') to consider further aspects of its cooperation arrangements and the home authority's supervision of the incoming CCP. The Bank's proposed expectations for this assessment are higher than for the Level 1 informed reliance assessment, given the greater UK interest in the CCP relative to other authorities and high proportion of UK resources committed to the CCP.

3.13 The Bank proposes that an incoming CCP that has been assessed as potentially systemically important and where the expectations of the applicable informed reliance assessment have been met will usually be determined as Tier 1.

3.14 The Bank proposes that an incoming CCP that has been assessed as potentially systemically important and where the expectations of the applicable informed reliance assessment have not been met will usually be determined as Tier 2.

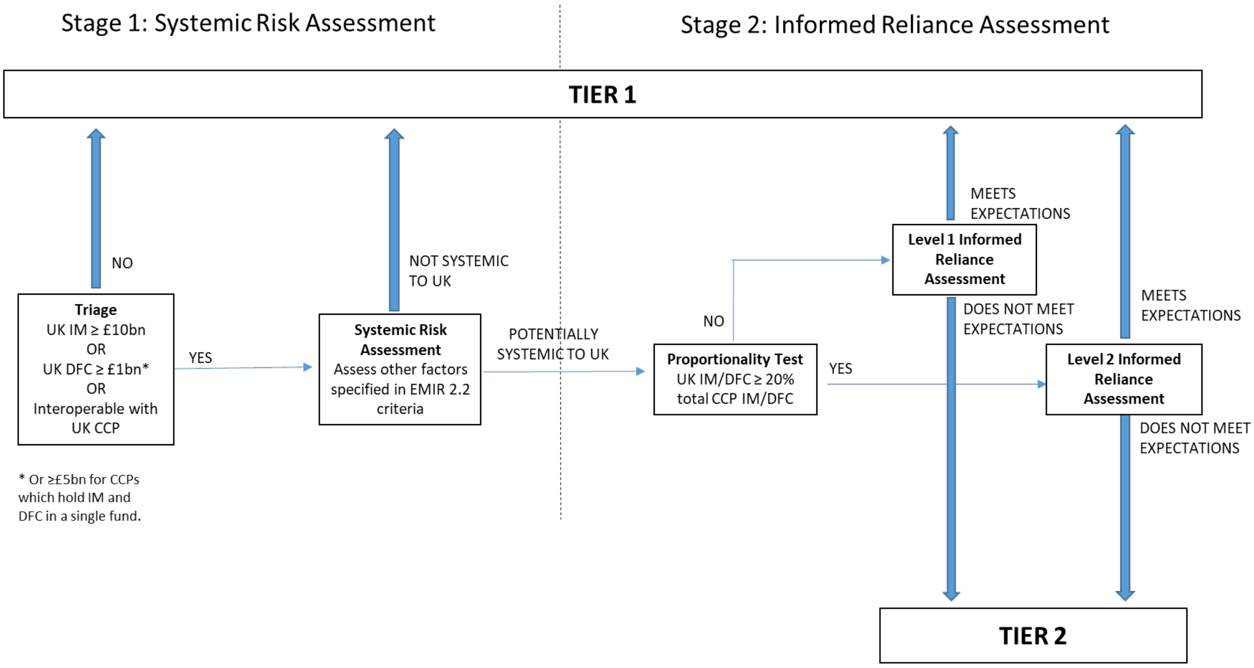
3.15 The determination of whether an incoming CCP is Tier 2 (or not) would depend on the outcome of the applicable informed reliance assessment along with the other factors considered in the tiering process (i.e. initial triage, systemic risk assessment, proportionality).

3.16 The Bank does not envisage at present recommending the use of location regulations or 'Tier 3' as part of this framework.

3.17 Figure 1 below illustrates the Bank's proposed approach to tiering incoming CCPs.

12 As specified by EMIR Article 27.7 and EMIR Article 25(2)(c).

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



Implementation

3.18 The Bank proposes that the implementation date for the final policy will be Friday 1 July 2022.

Responses and next steps

3.19 This consultation closes on Friday 25 February 2022. The Bank invites feedback on the proposals set out in this consultation. Please address any comments or enquiries to FMIFeedback@bankofengland.co.uk.

3.20 The Bank is concurrently consulting on its approach to assessing comparable compliance[13]. In due course the Bank will also consult on its approach to setting fees for incoming CCPs.

3.21 The proposals set out in this CP have been designed in the context of the UK having left the European Union and the transition period having come to an end. Unless otherwise stated, any references to EU or EU derived legislation refer to the version of that legislation which forms part of retained EU law.[14]

13 Under EMIR Article 25a(1), Tier 2 CCPs may submit a reasoned request to the Bank for comparable compliance. Comparable Compliance, where granted, allows a Tier 2 CCP to satisfy compliance with certain EMIR requirements by complying with a comparable requirement in the home authority jurisdiction, avoiding the Tier 2 CCP having to comply with both requirements.

14 For further information please see www.bankofengland.co.uk/eu-withdrawal/transitioning-to-post-exit-rules-and-standards.

4 Proposals

4.1 This section sets out the Bank's proposed approach to tiering decisions as part of the recognition process for incoming CCPs and how this approach relates to the requirements as set out in EMIR.

4.2 The Bank proposes a two-stage process to identifying whether an incoming CCP should be determined as a Tier 1 or Tier 2 CCP. The process proposed in this CP is designed to be aligned with the Bank's high-level approach to incoming supervision (see paragraphs 2.10-2.17). It is also designed to be 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).

4.3 No individual assessment criteria will, in isolation, be considered decisive in the Bank's tiering decisions. The Bank's determinations will be made on the basis of a holistic assessment of all applicable criteria, as detailed in this CP.

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

4.5 Incoming CCPs are not required to submit information relating to tiering at this stage, but may continue to submit recognition applications to the Bank in accordance with UK Binding Technical Standards 153/2013[15]. The Bank will write separately to incoming CCPs to request this information when the Bank is ready to begin its tiering assessments to ensure that the information provided is appropriate and up-to-date.

Stage 1: Systemic Risk Assessment

4.6 The Bank proposes to use the following indicators to 'triage' incoming CCPs that are potentially systemic to UK financial stability when they apply for recognition to provide clearing services to clearing members established in the UK:

- **Initial Margin (IM):** Whether the incoming CCP has held at least £10bn of UK clearing member IM (including non-UK subsidiaries of UK headquartered firms) across all services, at any point in the last 5 years. This IM figure is inclusive of any margin add-ons and any IM clearing members post on behalf of clients;

- **Default Fund Contribution (DFC)**: Whether the incoming CCP has held at least £1bn[16] of UK clearing member DFCs (including non-UK subsidiaries of UK headquartered firms) across all services at any point in the last 5 years; or

- **Interoperability:** Whether the incoming CCP has an interoperability arrangement in place with a UK CCP.

4.7 The Bank expects that an incoming CCP that does not satisfy any of these criteria will usually not progress to the next stage of the tiering assessment, and will be classified as a Tier 1 CCP under

[15] 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, as it forms part of retained EU law.

[16] Or £5bn for CCPs which hold IM and DFC in a single fund.

EMIR. An incoming CCP that satisfies one or more of these criteria will be subject to a more detailed systemic risk assessment.

4.8 In proposing to use three simple indicators, the Bank aims to provide visibility to incoming CCPs about whether they might be considered systemically important to UK financial stability, and reduce the administrative burden on CCPs that are most likely to be designated as Tier 1. These indicators also allow incoming CCPs to identify whether they are likely to be triaged and hence what information the Bank is likely to consider in order to make a tiering decision.

4.9 The Bank proposes that the triage criteria outlined in paragraph 4.6 are indicative. The Bank may use its judgement to opt to further assess the CCP before making a tiering determination, for example if it was close to one of more of the triage indicators.

4.10 For those incoming CCPs that meet one or more of the triage criteria, the Bank proposes to undertake a more detailed systemic risk assessment in order to assess factors relating to the incoming CCP that may impact its systemic importance to the UK and ensure the triage criteria correctly identified the incoming CCP as potentially systemic for UK financial stability. This will include assessing the criteria outlined in EMIR Article 25(2a). Those indicators the Bank deems most important for this assessment are listed in paragraph 4.13 below. The Bank proposes to 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 CP explains the rationale for each key indicator against the relevant criteria within EMIR Article 25(2a).

4.11 The objective of the systemic risk assessment is to verify whether an incoming CCPs that has met the triage thresholds is potentially systemic for UK financial stability, by carrying out a more detailed analysis of the incoming CCP. This assessment will also consider, amongst other things, the diversity in approaches to margin models and default waterfalls.

4.12 The Bank proposes that if this more detailed assessment indicates that an incoming CCP is not systemic to UK financial stability, the incoming CCP will be classified as Tier 1 (and will therefore not progress to Stage 2). Tier 1 CCPs will be required to meet the recognition requirements in EMIR. These include i) HM Treasury making a determination that the home authority's legal and supervisory frameworks are equivalent to UK requirements and effective and ii) the Bank establishing effective cooperation arrangements with relevant authorities meeting the minimum specifications set out in EMIR Article 25(7).

4.13 The Bank proposes to review the following non-exhaustive key indicators:

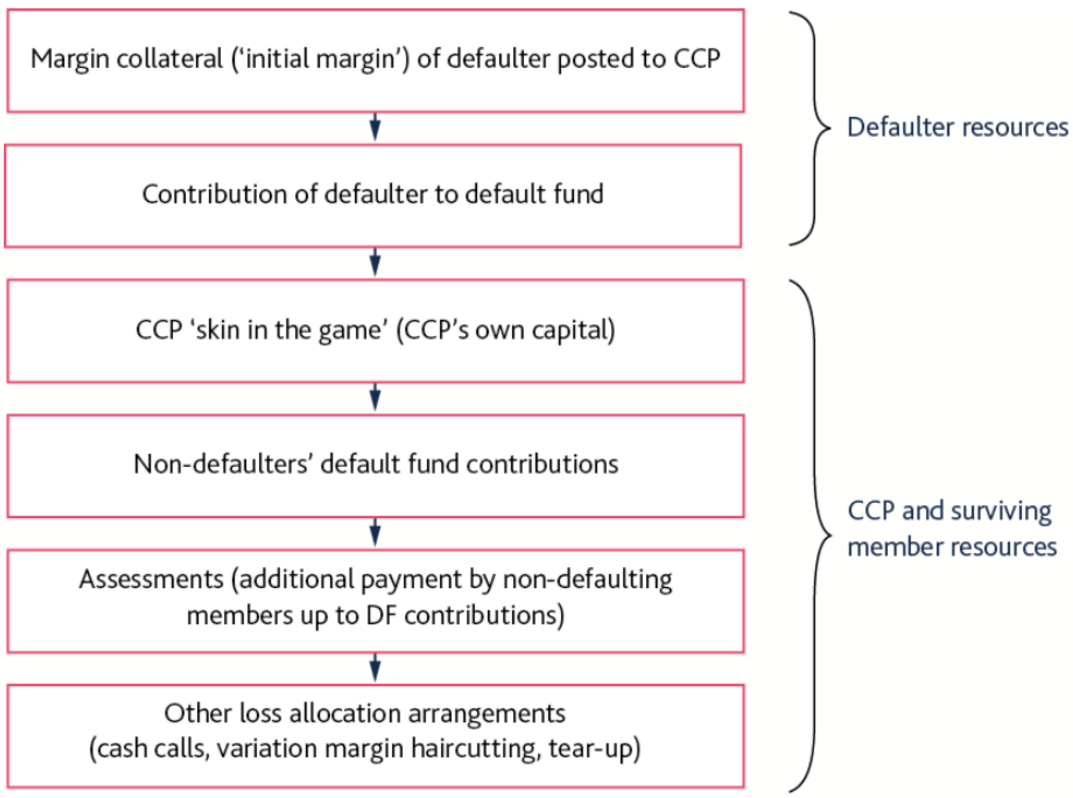
- Products cleared by the incoming CCP
- Margin, collateral, and default fund contributions
- The nature of the incoming CCP's access model
- Access to alternative clearing venues
- Interactions with other financial institutions.

4.14 Additional detail about the type of information the Bank proposes to review to make its determinations is set out in Annex 1 (Proposed Systemic Risk Assessment).

Explanation for proposed IM and DFC indicators

4.15 Both IM and the DFC are resources that form part of a CCPs default waterfall (Figure 2), and they can be used by the CCP to meet the obligations owed by defaulting clearing members to non-defaulting clearing members.

Figure 2: An illustrative CCP Default Waterfall



4.16 IM is collateral that is collected to cover potential changes in the value of a participant's position ('potential future exposure') over the time it would take to close the position in the event the participant defaults. Because IM is a measure of the potential risk of a position or portfolio of positions, the Bank considers the total amount of IM posted by UK clearing members to be a good indicator of how important a CCP is to UK clearing members and therefore the risks that would arise if it was unavailable. The Bank considers that the proposed £10bn threshold represents a significant proportion of UK IM with the potential to cause major losses to UK entities or disruption to UK financial stability.

4.17 The default fund is a pool of funds contributed to by all clearing members. It can be used to absorb losses that occur when a clearing member defaults on its obligations to the CCP and the resources provided by the defaulting party (or parties) are not sufficient to cover the losses incurred by the CCP. Therefore DFC of UK clearing members is a measure of the contributions (assets) UK clearing members have at risk at a CCP if a loss is mutualised (as shown in 'Figure 2: An illustrative CCP Default Waterfall' above, total clearing member losses may exceed their DFC if CCPs call for additional amounts of DFC or use other arrangements such as haircutting variation margin to allocate losses). The Bank considers that the proposed £1bn threshold represents a significant potential liability of UK firms.

4.18 Therefore, the Bank proposes to use both the IM and DFC metrics as indicators of potential systemic risk because a high aggregate value in either could indicate systemic importance to UK financial stability.

4.19 The Bank is aware that some CCPs hold initial margin and default fund contributions in a single fund, and hence default fund contributions are of similar size to initial margin. The Bank recognises that in this case the size of the UK DF is likely to overstate the CCPs systemic importance to the UK. Therefore where IM and DFC is held in the same fund, the Bank proposes to set a higher threshold of £5bn of UK clearing member default fund across all services at any point in the last 5 years.

4.20 The Bank proposes that the calculation of UK IM and DFC should include that attributable to non-UK subsidiaries of UK headquartered firms. This is because it is possible that UK headquartered firms may be clearing business either partially or entirely through non-UK subsidiaries. Disruption to an incoming CCP could have an impact on UK financial stability through the impact on non-UK subsidiaries where contagion effects could impair balance sheets of UK headquartered firms.

4.21 The Bank proposes a 5-year lookback period for the IM and DFC calculations to allow the Bank to consider periods of stress where requirements may rise. The Bank considers this important to ensure that the 'triaging' metrics reflect the maximum UK clearing activity within an incoming CCP over a period of time.

Explanation for proposed Interoperability with UK CCPs criteria

4.22 Interoperability arrangements offer advantages by improving market access and allowing clearing members to participate in multiple markets without incurring the costs associated with multiple CCP memberships. However, CCPs' interoperability arrangements could introduce the risk of inter-CCP contagion, with issues at an incoming CCP having the potential to transmit to the interoperable UK CCP and its membership. Contagion can occur due to an issue with the linked incoming CCP itself, or the incoming CCPs' clearing members. This means that CCPs within the interoperability arrangement may be exposed to the weak risk management and other practices (e.g. margin methodologies; membership standards) of the other. The operational complexities of an interoperability agreement may also increase operational risk and reduce transparency.

Stage 2: Proportionality and Informed Reliance Assessment

4.23 Where an incoming CCP is considered potentially systemically important to the UK according to the Stage 1 assessment, the Bank proposes to conduct an assessment to determine the extent to which the Bank is able to rely on the incoming CCP's home regulatory and supervisory authorities. We refer to these assessments as 'informed reliance assessments'.

4.24 The Bank proposes to conduct the informed reliance assessment in a proportionate manner commensurate with the Bank's approach to cross-border CCP supervision. Therefore, the Bank proposes to apply two different levels of informed reliance assessment, depending on the UK interest in a CCP relative to other authorities.

4.25 The Bank proposes a proportionality test to assess the proportion of i) IM and ii) DFC attributable to UK clearing members (including non-UK subsidiaries of UK headquartered firms) prior to the informed reliance assessment. The Bank proposes to set the proportionality thresholds at 20% of the incoming CCP's total IM and DFC. This would be calculated based on a 5-year average of IM and DFC across all services at the incoming CCP.

4.26 Depending on the outcome of proportionality test, the Bank proposes to apply one of two different levels of informed reliance assessment: either a 'Level 1 informed reliance assessment' or a more intensive 'Level 2 informed reliance assessment'.

4.27 Where both the IM and DFC attributable to UK clearing members (or subsidiaries of UK headquartered clearing members) is below 20%, the Bank proposes to undertake a 'Level 1 informed reliance assessment'. This assessment would consider what level of supervisory cooperation is essential in order for the Bank to be able to place reliance on the home authority's regulation and supervision.

4.28 The Bank proposes that an incoming CCP that is below the proportionality test threshold, and where the Bank's expectations for the Level 1 informed reliance assessment have been met, will usually be determined as Tier 1.

4.29 Where either or both IM and DFC attributable to UK clearing members (or subsidiaries of UK headquartered clearing members) is at or above 20%, the Bank proposes to subject the incoming CCP to a more intensive 'Level 2 informed reliance assessment'. The Bank's proposed expectations for this assessment are higher than for the Level 1 informed reliance assessment, given the greater UK interest in the CCP relative to other authorities.

4.30 The Bank proposes that an incoming CCP that is above one or both of the proportionality assessment thresholds, and where the Bank's expectations for the Level 2 informed reliance assessment have been met, would usually be determined as Tier 1.

4.31 The Bank proposes that an incoming CCP that is potentially systemically important, and where the Bank's expectations for the applicable informed reliance assessment have not been met, would usually be determined as Tier 2.

4.32 The determination of whether an incoming CCP is Tier 2 would depend on the outcome of the applicable informed reliance assessment along with the other factors considered in the tiering process (i.e. initial triage, systemic risk assessment, proportionality).

Explanation for proposed proportionality test and corresponding informed reliance assessments

4.33 The two levels of informed reliance assessments reflect the Bank's approach to proportionality leading to different expectations for the depth of informed reliance depending on the UK's interest and resources at risk in the systemically important CCP relative to other authorities.

4.34 The Bank considers that such a proportionality approach to informed reliance assessments is consistent with the 2009 G20 Pittsburgh Summit agreement[17]. Central clearing is critical to managing risk throughout financial markets, but can only be fully achieved where international regulators work together towards a common goal. It is important for financial stability that globally significant CCPs do not have 'too many hands on the wheel' when it comes to regulation and supervision. The Bank considers that this proportionate approach supports effective cooperation among financial regulators and bolsters the safety and utility of global clearing markets.

4.35 Equally relevant, where an incoming CCP's DFC represents a larger host jurisdictional interest (in this case at or above 20%), the host jurisdiction would bear the greater burden in the event of CCP failure. Therefore, the Bank considers it is reasonable to require a greater level of assurance that the home authority is delivering robust and equivalent supervisory outcomes.

4.36 For incoming CCPs that are considered potentially systemically important to the UK and where the UK represents a significant proportion of the CCP business, the Bank proposes it is appropriate to require more information and closer co-operation in order rely on the home authority for supervision and regulation of the CCP to achieve the Bank's financial stability objective. This is why the 'Level 2 informed reliance assessment' considers more factors, at greater depth, than those covered by the 'Level 1 informed reliance assessment'.

Contents of the informed reliance assessments

4.37 For incoming CCPs that are considered potentially systemically important to the UK, the Bank proposes to consider the following for both levels of informed reliance assessments:

- 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 the relevant home authorities[18], including, where appropriate, co-operation arrangements and transparency around the regulation and supervision of the incoming CCP.

4.38 These factors are consistent with Principles for Financial Market Infrastructure, Responsibility E[19], and therefore reflect globally accepted standards and expectations of supervisory and regulatory cooperation.

17 G20 Leaders Statement: The Pittsburgh Summit.

18 Any relevant national or international authority which may, in the Bank's judgement, have a significant impact on the regulatory and supervisory framework of the incoming CCP; and/or the supervisory outcome of the incoming CCP.

19 PFMIs Responsibility E: Cooperation with other authorities Central banks, market regulators, and other relevant authorities should cooperate with each other, both domestically and internationally, as appropriate, in promoting the safety and efficiency of FMIs.

4.39 The Bank proposes to take home authorities' regulatory and supervisory priorities into consideration, including whether the authorities responsible for regulating and supervising globally systemic CCPs act in the interests of protecting financial stability.

4.40 For existing relationships with relevant home regulatory and supervisory authorities, the Bank proposes to consider the effectiveness of the co-operative framework it already has in place with that authority.

4.41 For home regulatory and supervisory authorities where the Bank has little or no previous bilateral relationship, the Bank proposes that an informed reliance assessment would consider whether, in the judgement of the Bank, an effective co-operative relationship is likely to develop with the home authorities. This would be determined on the basis of the same key factors as outlined in the table below.

4.42 To the extent possible, the Bank proposes to rely on information submitted as part of the equivalence process. As a result, this CP focuses on how the Bank proposes to assess its relationship with the relevant home authorities, including, where appropriate, co-operation agreements and transparency around the home authority regulatory and supervisory approach as they relate to incoming CCPs.

4.43 The key areas the Bank proposes to review when assessing the extent to which the Bank is able to rely on the relevant home authorities are outlined in the table below. This list is 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 informed reliance assessment. In order to aid its review the Bank may also request information and/or clarifications from the relevant home authorities.

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)**	**Rationale**
Regulatory cooperation			
Engagement with the relevant home authorities	• Does the Bank receive notification of relevant regulatory developments, including those that may materially affect the rules or procedures of the CCP? • Does the Bank consider the regulatory cooperation to be open and effective?	• Does the Bank receive early or advance notification of new and material changes to regulations affecting the CCP?	• To provide assurance that the Bank will have dialogue on regulatory changes affecting the CCP in the home jurisdiction that could impact UK financial stability.

Supervisory cooperation			
Engagement with the relevant home authorities	• Does 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: ○ Bi-lateral meetings at principal and working-level. ○ Participation in supervisory colleges, where applicable. ○ For interoperable CCPs, participation in interoperable roundtable. • Does the Bank consider the supervisory cooperation to be open and effective?	• Does 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 one or more of the following: ○ 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 number of supervisory visits or to conduct occasional joint supervisory examinations (at least annually).	• To provide assurance over the extent to which the Bank's priorities align with those of the relevant home authorities and, where there are material differences, the extent to which the Bank has the ability to influence the relevant home authorities.
Supervisory aims and priorities	• Does the Bank have a sound understanding of the relevant home authorities' supervisory approach and priorities as they apply to the CCP?	• To what extent do the relevant home authorities' supervisory priorities for the CCP align with the Bank's priorities? • Does the Bank have confidence that the relevant home authorities will include	

		the Bank's views as a source of input[20] into its decision-making when setting its priorities?	
Information Sharing			
	• Do the relevant home authorities share relevant information regarding the CCP with the Bank in a timely manner? • Does 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 (e.g. model changes, extension of services etc). • Do the relevant home authorities notify the Bank promptly of material events to the CCP?	• More detailed information sharing. This might include (but is not limited to): ○ 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.	• To provide assurance that the home jurisdiction is achieving broadly equivalent supervisory outcomes to the Bank in relation to the CCP.
Crisis management			
	• Where applicable, have the relevant home authorities shared	• Does the Bank participate in a crisis management group (or	• To provide assurance that the relevant

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

	enough relevant information about the CCP with the Bank in a timely manner during previous crises? • If not, does the Bank have confidence that the relevant home authorities would share timely, relevant information?	equivalent) operated by the home jurisdiction, where the CCP is discussed? • If not, does the Bank have confidence that it will be invited to participate in the crisis management group?	home authorities' approach to crisis management and resolution is broadly aligned with that of the Bank.
Other considerations			
Dispute resolution	• Does the Bank have acceptable dispute resolution procedures with the relevant home authorities?		
Engagement with international standards	• What is the extent to which the home jurisdiction has engaged and committed to international regulatory fora, such as the Committee for Payments & Market Infrastructure (CPMI) or International Organization of Securities Commissions (IOSCO)?		• To provide assurance that the jurisdiction of the relevant home authorities will consider global consequences to regulatory action.
Regulatory environment	Overall assessment of cooperative nature of relevant home authorities, including to what extent do the relevant home authorities have policies in place that may influence the likelihood of the CCP becoming systemically important to the UK?		• To capture regulatory factors that may increase the UK's interest in an incoming CCP.

5 Reviewing Tiering Decisions

5.1 The Bank may review an existing tiering decision if there is a significant change which impacts the incoming CCP's risk profile.

5.2 The Bank proposes that where it has reason to believe that there has been a change in the criteria outlined in Stage 1 or Stage 2 of the assessment, it may request updated information periodically to provide assurance that the incoming CCP is appropriately tiered.

5.3 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.

6 Comparable compliance for Tier 2 CCPs

6.1 Incoming CCPs that are designated Tier 2 will be subject to additional requirements to Tier 1 CCPs. In addition to the recognition requirements for Tier 1 CCPs, Tier 2 CCPs will also be required to meet certain EMIR standards[21] and will be subject to direct supervision by the Bank.

6.2 Under EMIR Article 25a(1), Tier 2 CCPs may submit a reasoned request that the Bank assesses whether in its compliance with the applicable third-country framework, taking into account the equivalence decisions made by the HMT, that CCP may be deemed to satisfy compliance with the requirements set out in EMIR Article 16 and Titles IV and V.

6.3 The Bank is concurrently consulting on its approach to assessing comparable compliance in a separate CP.

Annex 1: Proposed Systemic Risk Assessment

EMIR Art 25(2a) criteria	Proposed Bank review area	Rationale	Proposed information for 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 Art 25(2a)(a))	• Products cleared by the incoming CCP.	• Different attributes of the product may impact the risk profile of the CCP. • Complex or illiquid products can be difficult to price and therefore increase the risk and complexity of a CCPs model. Whereas, plain vanilla products would result in less risk as they are transparent and more easily priced.	• 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	• Margin, collateral, and default fund contributions.	• Reviewing breakdowns of IM, DFC and total collateral held by the CCP will enable the Bank to identify any additional risks to UK financial stability, for example large concentrations of a	• The total default fund contributions held by the incoming CCP, by currency. • The default fund contributions made to the incoming CCP by UK clearing members (including

21 Article 16 on capital requirements, Titles IV on Requirements for CCPs and Title V on interoperability arrangements.

stability of the UK (EMIR Art 25(2a)(b))		particular asset class. • The Bank will also consider any aspects of the incoming CCP's IM or DFC methodology, which may make the triage indicators unrepresentative of risk to UK financial stability or inconsistent with the metrics of other CCPs.	overseas subsidiaries of UK headquartered firms), by currency. • The total IM held by the incoming CCP in total by underlying asset, currency, and split between house and client accounts. • The total IM and 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 Art 25(2a)(c))	• The nature of the incoming CCP's access model.	• A CCP's membership structure is important to the extent that it potentially increases the risk that the CCP poses to UK financial stability, or potentially limits access to markets that are important for UK participants.	• Access model and membership requirements. • The extent to which UK clients access the non-UK CCP via UK clearing members (including non-UK subsidiaries of UK headquartered firms) and non-UK clearing members.
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	• Access to alternative clearing venues.	• Disruption to an incoming CCP may result in a UK financial stability issue via disruption to the clearing of services used by UK clearing members. This risk can be	• 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

established in the UK (EMIR Art 25(2a)(d))		partially mitigated if alternative venues are reasonably accessible.	alternative venues. • Whether the products offered are subject to the mandatory clearing obligation.
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 Art 25(2a)(e))	• Outsourcing and third-party service providers. • Interoperability with UK CCPs.	• The failure of a critical service provider could be a significant UK financial stability event if it impact the core services provided by a CCP. • The default of an incoming CCP would be a serious financial stability event with the contagion effect potentially spread to a UK CCP by the existence of an interoperable link.	• A list of critical service providers and the services they are responsible for delivering. • The materiality of transactions cleared via the interoperability agreement, relative to the overall size of the business of the UK CCP in the interoperability agreement.

BANK OF ENGLAND

Appendix: Draft Statement of Policy: The Bank of England's approach to tiering incoming central counterparties

Draft Statement of Policy

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

November 2021

Contents

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 ([22]), and relevant home authorities.

1.2 Following the UK’s withdrawal from the EU, the UK has retained the EU framework for recognising incoming CCPs (known as ‘EMIR 2.2’[23]). EMIR 2.2 requires the Bank to “tier” incoming CCPs on the basis of whether the CCP is systemically important, or likely to become systemically important, for the financial stability of the UK. Where this is not the case, the CCP will be categorised as ‘Tier 1`; where this is the case, the CCP will be categorised as ‘Tier 2’ and will become subject to direct UK supervision and regulation.

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 determinations.

Implementation

1.4 The Bank will implement its approach to tiering from Friday 1 July 2022.

[22] Including those currently in the Temporary Recognition Regime For the full list see here.

[23] 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.

2 Definitions

Tiering

2.1 Tiering is the classification of individual incoming CCPs according to the level of systemic importance or likely systemic importance for the financial stability of the UK. An incoming CCP that does not meet this threshold is categorised as 'Tier 1' CCP, and is primarily supervised and regulated by its home authority. If the Bank determines that an incoming CCP is or is likely to become systemically important for UK financial stability – the Bank can subject that CCP to direct UK supervision and regulation ('Tier 2' CCP).

Initial Margin

2.2 Initial Margin (IM) is collateral that is posted by the CCPs' 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 using the term IM in this SoP, the Bank includes margin add-ons and IM posted by clearing members on behalf of clients (regardless of the jurisdiction of those clients).

Default Fund Contribution

2.3 The 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.

Interoperability

2.4 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.

Informed reliance assessment

2.5 Informed reliance assessment is the process whereby the Bank will determine the extent to which the Bank is able to rely on the home authority for supervision and regulation of the incoming CCP, where risks can be mitigated, as described in 'Stage 2: Informed Reliance Assessment'.

Incoming CCP

2.6 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.

Relevant Home Authorities

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

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

3 The Bank's approach to tiering incoming CCPs

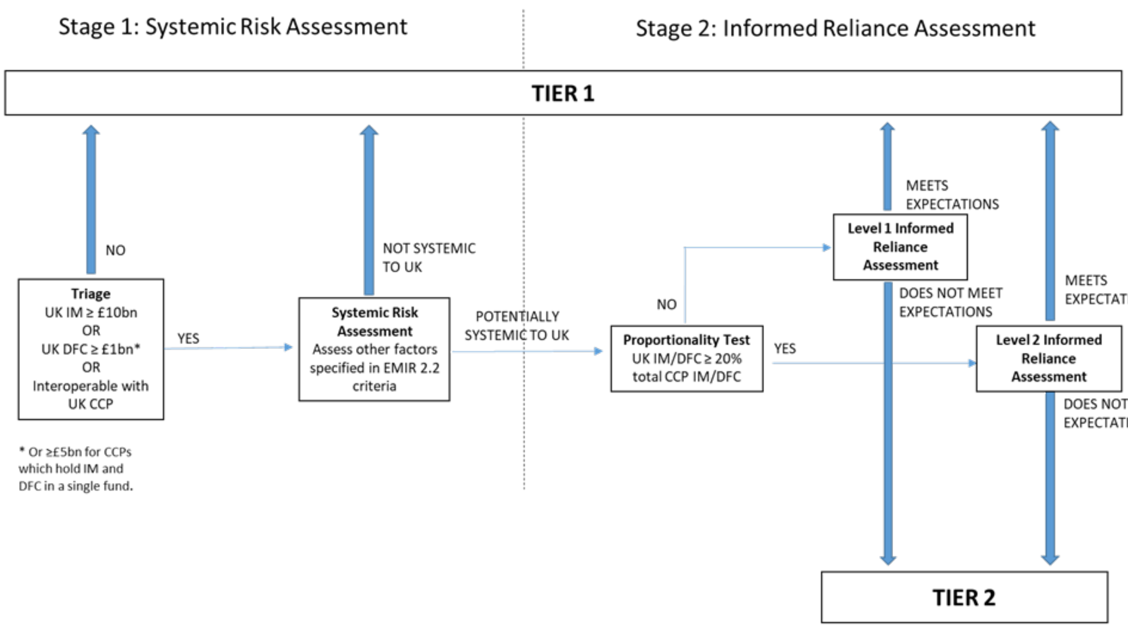
3.1 The Bank will undertake a two-stage process to identifying whether an incoming CCP should ultimately be determined as a Tier 1 or Tier 2 CCP. The process is consistent with the statutory framework for the Bank to determine whether an incoming CCP is systemically important or likely to become systemically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

3.2 No individual assessment criteria detailed in this SoP will, in isolation, be decisive in the Bank's tiering determinations. The Bank's determinations will be made on the basis of a holistic assessment of all applicable criteria.

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

3.4 The flow 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: Systemic Risk Assessment

3.5 The Bank will assess the following indicators to 'triage' incoming CCPs that are potentially systemic to UK financial stability when they apply for recognition to provide clearing services to clearing members established in the UK:

- **Initial Margin (IM):** Whether the incoming CCP has held at least £10bn of UK clearing member IM (including non-UK subsidiaries of UK headquartered firms) across all services, at any point in the last 5 years. This IM figure is inclusive of any margin add-ons and inclusive of IM clearing members post on behalf of clients;

- **Default Fund Contribution (DFC)**: Whether the incoming CCP has held at least £1bn[24] of UK clearing member DFCs (including non-UK subsidiaries of UK headquartered firms) across all services at any point in the last 5 years; or

- **Interoperability:** Whether the incoming CCP has an interoperability arrangement in place with a UK CCP.

3.6 An incoming CCP that does not satisfy any of these criteria will usually not progress to the next stage of the tiering assessment, and will be classified as a Tier 1 CCP under EMIR. An incoming CCP that satisfies one or more of these criteria will be subject to a systemic risk assessment.

3.7 The triage criteria outlined in paragraph 3.5 are indicative only. Thus the Bank may use its judgment to opt to further assess the CCP before making a tiering determination, for example, if the CCP is close to one or more of the triage indicators.

3.8 For those incoming CCPs that meet one or more of the triage criteria, the Bank will undertake a more detailed systemic risk assessment in order to assess factors relating to the incoming CCP that may impact its systemic importance to the UK and ensure the triage criteria correctly identified the incoming CCP as potentially systemic for UK financial stability. This will include assessing the criteria outlined in EMIR Article 25(2a).

3.9 Those indicators the Bank deems most important for this assessment are listed in 3.11 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 approaches to margin models and default waterfalls.

3.10 If this more detailed assessment indicates that an incoming CCP is not likely systemically important to UK financial stability, the incoming CCP will be classified as Tier 1 (and will therefore not progress to Stage 2).

3.11 The Bank will review the following non-exhaustive 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

- Interactions with other financial institutions.

3.12 Additional detail about the type of information it will review to make its determinations is set out in Annex 1 (Systemic Risk Assessment).

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24 Or £5bn for CCPs which hold IM and DFC in a single fund.

Stage 2: Informed Reliance Assessment

3.13 Where an incoming CCP is considered potentially systemically important to the UK according to the Stage 1 assessment, the Bank will conduct an assessment to determine the extent to which the Bank is able to rely on the incoming CCP's home regulatory and supervisory authorities ('informed reliance assessment').

3.14 The Bank will apply two levels of informed reliance assessments, depending on the UK interest in a CCP relative to other authorities.

3.15 The Bank will conduct a proportionality 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) prior to the informed reliance assessment. The Bank has set the proportionality thresholds at 20% of the incoming CCP's total IM and DFC. This will be calculated based on a 5-year average of IM and DFC across all services at the incoming CCP.

3.16 Depending on the outcome of the proportionality test, the Bank will apply one of two different levels of informed reliance assessment: either a 'Level 1 informed reliance assessment' or a 'Level 2 informed reliance assessment'.

3.17 Where both the IM and DFC attributable to UK clearing members (or subsidiaries of UK headquartered clearing members) is below 20%, the Bank will undertake a 'Level 1 informed reliance assessment'. This assessment will consider what level of supervisory cooperation is essential in order for the Bank to be able to place reliance on the home authority's regulation and supervision.

3.18 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 usually be determined as Tier 1.

3.19 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%, the Bank will subject the incoming CCP to a 'Level 2 informed reliance assessment'.

3.20 An incoming CCP that is above one or both of the proportionality assessment thresholds and where the Bank's expectations for the Level 2 informed reliance assessment have been met, will usually be determined as Tier 1.

3.21 An incoming CCP that is potentially systemically important for UK financial stability, and where the Bank's expectations of the applicable informed reliance assessment have not been met, will usually be determined as Tier 2.

3.22 The determination of whether an incoming CCP is Tier 2 will depend on the outcome of the applicable informed reliance assessment along with the other factors considered in the tiering process (i.e. initial triage, systemic risk assessment, proportionality).

Contents of the informed reliance assessments

3.23 For incoming CCPs that are considered potentially systemically important to the UK, the Bank will consider the following for both levels of informed reliance assessments:

- 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 the relevant home authorities, including, where appropriate, co-operation arrangements and transparency around the regulation and supervision of the incoming CCP.

3.24 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.

3.25 For existing relationships with relevant home regulatory and supervisory authorities, the Bank will consider the effectiveness of the co-operative framework it already has in place with that authority.

3.26 For home regulatory and supervisory authorities where the Bank has little or no previous bilateral relationship, 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 same key factors as outlined in the table below.

3.27 To the extent possible, the Bank will rely on information submitted as part of the equivalence process.[25]

3.28 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 below. This list is 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 informed reliance assessment. In order to aid its review the Bank may also request information and/or clarifications from the relevant home authorities.

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 cooperation		
Engagement with the relevant home authorities	• Does the Bank receive notification of relevant regulatory developments, including those that may materially affect the rules or procedures of the CCP? • Does the Bank consider the regulatory	• Does the Bank receive early or advance notification of new and material changes to regulations affecting the CCP?

[25] Under UK EMIR Article 25(6) HM Treasury is responsible for determining the home-country 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.

	cooperation to be open and effective?	
Supervisory cooperation		
Engagement with the relevant home authorities	• Does 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: ○ Bi-lateral meetings at principal and working-level ○ Participation in supervisory colleges, where applicable. ○ For interoperable CCPs, participation in interoperable roundtable. • Does the Bank consider the supervisory cooperation to be open and effective?	• Does 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 one or more of the following: ○ 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 number of supervisory visits or to conduct occasional joint supervisory examinations (at least annually).
Supervisory aims and priorities	• Does the Bank have a sound understanding of the relevant home authorities' supervisory approach and priorities as they apply to the CCP?	• To what extent do the relevant home authorities' supervisory priorities for the CCP align with the Bank's priorities? • Does the Bank have confidence that the relevant home authorities will include the Bank's views as a source of input[26] into its decision-making when setting its priorities?
Information sharing		

[26] This should not undermine the primacy of the relevant home authority and should be proportionate.

<table>
<tr><td></td><td>Do the relevant home authorities share relevant information regarding the CCP with the Bank in a timely manner?
Does 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 (e.g. model changes, extension of services etc).
Do the relevant home authorities notify the Bank promptly of material events to the CCP?</td><td>More detailed information sharing. This might include (but is not limited to):
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.</td></tr>
<tr><td>Crisis management</td><td colspan="2"></td></tr>
<tr><td></td><td>Where applicable, have the relevant home authorities shared enough relevant information about the CCP with the Bank in a timely manner during previous crises?
If not, does the Bank have confidence that the relevant home authorities would share timely, relevant information?</td><td>Does the Bank participate in a crisis management group (or equivalent) operated by the home jurisdiction, where the CCP is discussed?
If not, does the Bank have confidence that it will be invited to participate in the crisis management group?</td></tr>
<tr><td>Other considerations</td><td colspan="2"></td></tr>
<tr><td><u>Dispute resolution</u></td><td colspan="2">Does the Bank have acceptable dispute resolution procedures with the relevant home authorities?</td></tr>
</table>

Engagement with international standards	What is the extent to which the home jurisdiction has engaged and committed to international regulatory fora, such as the Committee for Payments & Market Infrastructure (CPMI) or International Organization of Securities Commissions (IOSCO)?
Regulatory environment	Overall assessment of cooperative nature of relevant home authorities, including to what extent do the relevant home authorities have policies in place that may influence the likelihood of the CCP becoming systemically important to the UK?

4 Reviewing Tiering Decisions

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

4.2 Where the Bank has reason to believe that there has been a change in the criteria outlined in Stage 1 or Stage 2 of the tiering assessment, it may request updated information periodically to provide assurances that the incoming CCP continues to be appropriately tiered. Incoming CCPs are obliged to notify the Bank of any material changes affecting the conditions for recognition. [27]

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.

27 UK EMIR Article 25(4b).

Annex 1: 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 Art 25(2a)(a))	• Products cleared by the incoming CCP	• 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 Art 25(2a)(b))	• Margin, collateral, and default fund contributions	• The total default fund contributions held by the incoming CCP, by currency; • The default fund contributions 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 in total by underlying asset, currency, and split between house and client accounts. • The total IM and 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 Art 25(2a)(c))	• The nature of the incoming CCP's access model	• Access model and membership requirements. • The extent to which UK clients access the non-UK CCP via UK clearing members (including non-UK subsidiaries of UK headquartered firms) and non-UK clearing members.

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 Art 25(2a)(d))	• Access to alternative clearing venues	• 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.
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 Art 25(2a)(e))	• Outsourcing and third-party service providers • Interoperability with UK CCPs	• A list of critical service providers and the services they are responsible for delivering. • The materiality of transactions cleared via the interoperability agreement, relative to the overall size of the business of the UK CCP in the interoperability agreement.