



EBA Consultation Paper
on
Draft Regulatory Technical Standards
on
Capital Requirements for CCPs
(EBA/CP/2012/08)

London, 15.06.2012

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I. Responding to this Consultation

The EBA invites comments on all proposals put forward in this paper.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/ rationale proposed; and
- describe any alternative regulatory choices EBA should consider.

Please send your comments to the EBA by email to EBA-CP-2012-08@eba.europa.eu by 31.07.2012, indicating the reference 'EBA-CP-2012-08' in the subject field. Please note that comments submitted after the deadline, or sent to another e-mail address will not be processed.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please indicate clearly and prominently in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an e-mail message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.eba.europa.eu under the heading 'Legal Notice'.

II. Executive Summary

At the trilogue meeting of 9 February 2012, the European Parliament, the Council and the European Commission reached a political agreement on the Regulation of the European Parliament and the Council on over-the-counter (OTC) derivative transactions, central counterparties (CCPs) and trade repositories ('EMIR' or 'Regulation'). The European Parliament adopted EMIR on 29 March 2012¹. At the time of writing these lines, two texts of EMIR are available, the Council version of 11 April 2012² and the Parliament version of 29 March 2012. The two texts have been submitted to the jurist linguists who will need to reconcile them. A final text of the EMIR is not expected before August 2012.

The European Commission's (EC) proposals for the EMIR³ requires the EBA to draft regulatory technical standards (RTS) on the capital requirements for CCPs.

This consultation paper puts forward the EBA proposals on the above topic. The input from stakeholders will assist in the development of the RTS, to be drafted and submitted to the European Commission (EC) for endorsement in the form of a Commission Regulation, i.e. a legally binding instrument directly applicable in all member States of the European Union. The development of the draft RTS is also required to cover the analysis of the costs and benefits that those legal provisions will imply. It would be particularly important to contribute information that helps assessing the impact of the proposals on capital and the period necessary for CCPs to adapt their systems in order to be able to comply with the Regulation.

The considerations on capital requirements expressed in this paper are based on the international standards developed by CPSS-IOSCO⁴ and on Directives 2006/48/EC and 2006/49/EC of the European Parliament and of the Council, which together form the so-called 'Capital Requirements Directive' or CRD⁵.

The EBA's view is that according to the Regulation the capital of a CCP, including retained earnings and reserves, should be at all times at least equal to the sum of:

- i. the CCP's operational expenses during an appropriate time span for winding-down or restructuring its activities;

¹ www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=20120329&secondRef=TOC&language=EN

² <http://register.consilium.europa.eu/pdf/en/12/st06/st06399.en12.pdf>

³ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0484:FIN:EN:PDF>

⁴ Principles for financial market infrastructures, assessment methodology and disclosure framework, CPSS Publications No 101, April 2012: <http://www.bis.org/publ/cpss101.htm>.

⁵ The Council and the European Parliament are currently negotiating revisions to the CRD. These are in the form of a package made up of one revised Capital Requirements Directive or CRD IV and a new Capital Requirements Regulation or CRR, colloquially together referred to as the 'CRD IV/CRR proposals'.

- ii. the capital necessary to cover the overall operational - including legal - risk born by the CCP; and,
- iii. the capital necessary to cover credit, counterparty credit and market risks stemming from 'non-covered activities'⁶ that the CCP carries out.

Other business and legal risks, borne by the CCP might lead its competent authority to require additional capital, similarly to banks which may be subject to extra capital charge.

In the EBA's view, risk exposures and capital requirements should be calculated using approaches set out for banks by the CRD.

As provided for by Regulation No 1093/2010 of the European Parliament and Council establishing the EBA⁷, before submitting the draft RTS to the Commission, the EBA will conduct a public consultation and analyse the potential costs and benefits of the proposed standards. This consultation paper includes the proposed legal text of the provisions constituting the draft RTS, an explanation of the proposed measures and a cost-benefit analysis.

The consultation period for this consultation paper will end on 31 July 2012.

⁶ The definition of 'non-covered activities' is provided in article 2(2) of the draft RTS.

⁷ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L 331, 15.12.2010, p. 12.

III. Background and rationale

The Regulation lays out provisions with the view to increasing the safety and transparency of the over-the-counter (OTC) derivatives markets. It introduces a legal obligation to clear OTC derivatives transactions through central counterparties (CCPs) and establishes organisational, conduct of business and prudential requirements for CCPs to ensure that these institutions are robustly risk-managed and financially sound irrespective of the financial instruments cleared.

The primary function of a CCP is to act as an intermediary between the counterparties to a bilateral trade, so that the parties' bilateral trade is replaced by two separate trades of each of them with the CCP. In this way, the CCP takes on the risk of the potential loss to which a party could be exposed if its counterpart were to default. Where one counterparty defaults, the CCP acts in the place of the defaulted counterparty and makes good its payment obligations. Therefore, a CCP allows market participants to trade without being exposed to the risk of each other's default.

To limit its credit exposures, the Regulation requires a CCP to collect margins, to maintain a pre-funded default fund and to maintain dedicated own resources. These resources make up the 'default waterfall' of risk mitigants that a CCP uses to cover its losses upon the default of one of its clearing members. In covering its losses, a CCP will use firstly the margins posted by the defaulting clearing member; secondly, the default fund contributions of the defaulting clearing member; thirdly, its dedicated own resources; and finally the default fund contributions of non-defaulting clearing members. Under no circumstances will a CCP use margins posted by non-defaulting clearing members to cover its losses resulting from the default of another clearing member. The CCP's dedicated own resources cannot be used to meet the CCP's regulatory capital requirements.

Articles 41 to 44 of the Regulation prescribe the calculation of financial resources: margins, default fund and dedicated own resources. These articles also specify the requirements about the collection, maintenance and use of the collaterals. Under these Articles no additional capital is required to mitigate the CCP's credit exposures or the market risk of the collateral collected.

Additional capital is however required under Article 16(2) of the Regulation to mitigate, on the one hand against market risk, credit risk and counterparty credit risk arising from non-covered activities; and, on the other hand, to mitigate against operational risk arising from all activities of a CCP (including both covered and non-covered ones). Capital held to meet the CCP's regulatory capital requirement and the CCP's dedicated own resources is invested in cash and in financial instruments. Similarly, collateral provided by clearing members in the form of cash is invested in financial instruments or deposited through highly secure arrangements with authorised financial institutions or central banks. Collateral provided by clearing members in the form of financial instruments is deposited with operators of securities settlement systems or through highly secure arrangements with authorised financial institutions. The introduction of these capi-

tal requirements will also ensure that the risks inherent in these activities (investment or others) are monitored and adequately capitalised.

Having identified these risks, a CCP should hold capital, including retained earnings and reserves, that is at all times at least equal to the sum of: (i) its operational expenses during an appropriate time span for winding-down or restructuring its activities; (ii) its capital requirements for the overall operational risk; and (iii) its capital requirements for credit, counterparty credit and market risks stemming from non-covered activities it carries out. The Regulation delegates powers to the Commission to adopt regulatory technical standards (RTS) specifying these requirements; the EBA is expected to develop the draft RTS, in close cooperation with the ESCB and after consultation with the ESMA, and to submit the RTS to the Commission by 30 September 2012. In developing the proposals explained in this consultation paper, relevant parts of the CPSS-IOSCO Principles for Financial Markets Infrastructure and of the Capital Requirements Directives 2006/48/EC and 2006/49/EC have been considered.

The nature of RTS under EU law

These draft RTS are produced in accordance with Article 10 of EBA regulation⁸. According to Article 10(4) of EBA regulation, they shall be adopted by means of regulations or decisions.

According to EU law, EU regulations are binding in their entirety and directly applicable in all Member States. This means that, on the date of their entry into force, they become part of the national law of the Member States and that their implementation into national law is not only unnecessary but also prohibited by EU law, except in so far as this is expressly required by them.

Shaping these rules in the form of a Regulation would ensure a level-playing field by preventing diverging national requirements and would ease the cross-border provision of clearing services since different set of rules are currently applicable to CCPs located in different Member States.

⁸ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L 331, 15.12.2010, p. 12.

IV. Draft Regulatory Technical Standards on the capital requirements for CCPs

In between the text of the draft RTS that follows, further explanations on specific aspects of the proposed text are occasionally provided, which either offer examples or provide the rationale behind a provision, or set out specific questions for the consultation process. Where this is the case, this explanatory text appears in a framed text box.

The final numbering of the articles might change after the adoption of the EMIR and the CRR and the finalization of the consultation of this RTS.



EUROPEAN COMMISSION

Brussels, **XXX**
[...](2012) **XXX** draft

COMMISSION DELEGATED REGULATION (EU) No .../..

of **XXX**

on

**Capital requirements for Central Counterparties (CCPs)
according to the European Parliament and Council
Regulation (EU) No **[XXX]****

COMMISSION DELEGATED REGULATION (EU) No .../..-

of [date]

supplementing Regulation (EU) No xx/xxxx [EMIR] of the European Parliament and of the Council with regard to regulatory technical standards on CCP Capital Requirements

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (the “Regulation” and “EBA”); in particular Article 15 thereof,

Having regard to Regulation (EU) No xx/xxxx [EMIR] of the European Parliament and of the Council of [...] on over the counter (OTC) derivatives transactions, central counterparties and trade repositories, and in particular Article 16 (3) thereof,

Explanatory text for consultation purposes

We replicate here below Article 16 of the EMIR on capital requirements for CCPs, providing the mandate to the EBA.

Article 16

Capital requirements

1. A CCP shall have a permanent and available initial capital of at least EUR 7,5 million to be authorised pursuant to Article 14.

2. Capital, including retained earnings and reserves, of a CCP shall be proportional to the risk stemming from the activities of the CCP. It shall at all times be sufficient to ensure an orderly winding-down or restructuring of the activities over an appropriate time span and that the CCP is adequately protected against credit, counterparty, market, operational, legal and business risks which are not already covered by specific financial resources as referred to in Articles 41 to 44.

3. In order to ensure consistent application of this Article, EBA shall, in close cooperation with the ESCB and after consulting ESMA, develop draft regulatory technical standards specifying requirements regarding the capital, retained earnings and reserves of a CCP referred to in paragraph 2.

EBA shall, in close cooperation with the ESCB and after consulting ESMA, submit those draft regulatory technical standards to the Commission by 30 September 2012.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1095/2010.

Whereas:

- (1) This Regulation is based on the draft regulatory technical standards submitted by the European Supervisory Authority (European Banking Authority) to the European Commission.
- (2) The European Banking Authority (EBA) has worked in close collaboration with the European System of Central Banks (ESCB) and has consulted the European Securities and Markets Authority (ESMA) before submitting the draft technical standards on which this Regulation is based. It has also conducted open public consultations on the draft regulatory technical standards, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010.
- (3) Regulation (EU) No xx/xxxx⁹ [‘EMIR’] establishes, among other matters, prudential requirements for central counterparties (CCPs) to ensure that those CCPs are safe and sound and comply at all times with the capital requirements. Given that risks stemming from clearing activities are covered by specific financial resources (Art. 41 to 44 of the EMIR), such capital requirements should ensure that the CCP is at all times adequately capitalised against credit, counterparty, market, operational, legal and business risks stemming from the non-covered activities as defined in Article 2(2) and that it is able to conduct an orderly winding down or restructuring of its operations if necessary.
- (4) As the EMIR introduces a legal obligation to clear over-the-counter (OTC) derivatives transactions through CCPs, strong regard has been given, in defining these regulatory technical standards, to the prudential requirements applicable to credit institutions and investment firms since CCPs are exposed to the same kind of risks as these institutions. Further, relevant parts of the Principles for Financial Market Infrastructure issued by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions (‘CPSS-IOSCO Principles’) have been taken into account.
- (5) In order to ensure that they would be able to organise an orderly winding-down or restructuring of their activities, CCPs should hold sufficient financial resources to withstand operational expenses over an appropriate period of time. A CCP should be able during such a period of time to set up any kind of arrangement in order to reorganise its critical operations, including recapitalising, replacing management, revising its business strategies, cost or fee structures, restructuring the services it provides, liquidating its clearing portfolio or merging with - or transferring its clearing activities to - another CCP.
- (6) Regulation (EU) No xxxx/2012 of the European Parliament and of the Council of xx ... 2012 on prudential requirements for credit institutions and investment firms¹⁰ seems to be an appropriate benchmark for the purpose of establishing capital requirements to

⁹ OJ...

¹⁰ OJ...

cover operational risk borne by CCPs, since the financial instruments the CCPs clear are the same as those used by credit institutions or investment firms. In accordance with Regulation (EU) No xxxx/2012 [CRR], the definition of operational risk in this Regulation includes legal risk.

- (7) Regulation (EU) No xxxx/2012 [CRR] seems to be an appropriate benchmark for the purpose of establishing capital requirements to cover risks stemming from non-covered activities carried out by CCPs, since these are very similar to those carried out by some credit institutions or investment firms.
- (8) It is necessary to establish ancillary tools to enable the competent authorities to verify that the capital of the CCP is sufficient at 'all times' as required by Art. 16 (2) of the EMIR. One such ancillary tool is the introduction of a notification threshold. Further, since reporting on capital requirements is required on a quarterly basis, it is desirable to fix the level of the notification threshold 25% higher than the capital requirements.
- (9) It is necessary to establish a floor to the estimation by the CCP of the time span for winding-down or restructuring its activities, that is conservative, and such a conservative floor is considered to be of twelve months' duration.
- (10) In order to assess the adequacy of the winding-down or restructuring periods taken into account in the calculation of the capital under Article 6 'Operational expenses for winding-down or restructuring', Article 5 'Information communicated to the competent authority' requires that detailed information is reported to the competent authorities in line with the Article 22 on the EMIR.
- (11) When establishing capital requirements to cover risks stemming from clearing activities, it is necessary to take into account the risk management framework that CCPs have set up in order to manage their risks, especially the procedures and mechanisms in place to deal with the default of a clearing member. In order to minimise the contagion risk of such a default, CCPs collect margins and maintain default funds and other financial resources to cover potential losses. It is assumed that the financial resources referred to in Articles 41 to 44 of Regulation (EU) No xx/xxxx [EMIR] can cover, in their entirety, credit, counterparty credit, market and liquidity risks stemming from the clearing activities of a CCP (or more precisely from clearing members' default management activities). As a consequence, capital requirements for risks stemming from clearing activities of a CCP should only cover the risks which are not covered by dedicated resources, i.e. operational, legal and business risks stemming from clearing activities.
- (12) Arrangements, strategies, processes and mechanisms implemented by a CCP to comply with Regulation (EU) No xx/xxxx ['EMIR'] need to be reviewed by its competent authority in accordance with its Article 21. In particular, the competent authority shall evaluate the risks to which the CCP is, or might be exposed and which are not addressed, or not fully addressed, by the application of the capital requirements set in Article 3. Those risks include for example reputation, strategic or business risks which may arise from the regulatory, economic or business environment. The competent authority shall ensure that an appropriate capital charge is applied in such cases. As a result of the review and evaluation of such risks - similar to Pillar 2 risks for credit institutions - the competent authority may, if deemed necessary, apply additional capital requirements or require the CCP to take the necessary actions or steps at an early stage to address the situation.

HAS ADOPTED THIS REGULATION:

Article 1

Subject matter and scope

This regulation lays down the detailed rules supplementing Article 16 of Regulation (EU) No xx/xxxx [‘EMIR’]. More in particular, it establishes rules relating to capital requirements for non-covered activities and capital requirements for operational risk for both covered and non-covered activities.

Article 2

Definitions

For the purpose of this Regulation, the following definitions shall apply:

- (1) ‘investment activities’ carried out by a CCP means investment of financial resources in accordance with Article 47 of Regulation (EU) No xx/xxxx [EMIR];
- (2) ‘non-covered activities’ means all activities which are not covered by the specific financial resources as set out in Articles 41 to 44 of Regulation (EU) No xx/xxxx [EMIR];
- (3) ‘winding-down or restructuring period’ means the number of months necessary for a CCP to ensure an orderly winding-down or restructuring of its activities, including re-organising its operations, recapitalising, replacing management, revising its business strategies, cost or fee structures, restructuring the services it provides, liquidating its clearing portfolio or merging with - or transferring its clearing activities to - another CCP.

Article 3

Capital requirements

Explanatory text for consultation purposes

The EBA considers that, in order to ensure that the capital will be available when needed, a CCP has to hold the sum of the resources necessary to cover each of the risks that have been identified in Article 16(2) of Regulation (EU) No xx/xxxx (‘EMIR’).

1. A CCP shall hold capital, including retained earnings and reserves, which shall be at all times more than or equal to the sum of:
 - (a) the CCP’s operational expenses during an appropriate time span for winding-down or restructuring its activities calculated in accordance with Article 6;
 - (b) the CCP’s capital requirements for operational risk calculated in accordance with Article 7;

- (c) the CCP's capital requirements for credit, counterparty credit and market risks stemming from its non-covered activities calculated in accordance with Article 8;
 - (d) the CCP's capital requirements for legal and business risks as set in Article 9.
2. The following items shall be deducted from the capital of a CCP:
- (a) contributions to any default fund of another CCP;
 - (b) financial resources referred to in Articles 43(1) and 45(4) of Regulation (EU) No xx/xxxx [EMIR] as long as they qualify as capital according to Article 2(26) of EMIR;
 - (c) resources which are not invested in accordance with Article 47(1) of the Regulation (EU) No xx/xxxx [EMIR] regulation.
3. A CCP may choose to hold more capital than required by this Regulation.

Article 4

Notification threshold

1. In the event that the amount of capital held by a CCP turns out to be lower than the threshold of 125% of the capital requirements ('notification threshold') set in Article 3, the CCP shall immediately notify the relevant competent authority.
2. That notification shall be made in writing and shall contain the following elements:
- (a) the reasons for the CCP's capital being below the notification threshold and a description of the short-term perspective of the CCP's financial situation;
 - (b) a comprehensive description of the measures the CCP intends to adopt to ensure the on-going compliance with the capital requirements.
3. On the basis of the information provided under paragraph 2, the competent authority shall decide whether to set a more stringent frequency for the CCP's reporting on its capital position with respect to the notification threshold.

Article 5

Information communicated to the competent authority

1. A CCP shall develop and maintain a general capital plan, to be updated annually, which shall:
- (a) specify how the CCP expects to raise new capital if its capital falls below the capital requirements set in Article 3,
 - (b) specify how the CCP could achieve an orderly winding-down or restructuring of its activities under the laws of the relevant jurisdictions over an appropriate time span in a way that avoids any systemic disruption to the markets or institutions supported by the CCP.

2. The general capital plan and its updates shall be approved by the competent authority in line with Article 22 of the EMIR.
3. In the event that the amount of capital held by a CCP falls below the capital requirements set in Article 3, the CCP shall immediately:
 - (a) inform its competent authority and provide the reasons for such a decline,
 - (b) indicate to its competent authority the relevant specific measures, of those included in the general capital plan, that it intends to activate in order to address the situation; and
 - (c) specify the timetable for their completion.
4. The general capital plan shall also include the estimation of the period for the winding-down or restructuring of the activities is sufficient to ensure, including in stressed market conditions, an orderly winding-down or restructuring of its activities, reorganising its operations, liquidating its clearing portfolio or transferring its clearing activities to another CCP. The estimation shall take into account the liquidity, size, maturity structure and potential cross-border obstacles of the positions of the CCP and the type of products cleared.

Article 6

Operational expenses for winding-down or restructuring

Explanatory text for consultation purposes

EBA considers that in order to ensure that a CCP holds sufficient capital to ensure an orderly winding-down or restructuring of its activities, the CCP should be required to provide its competent authority with an estimation of the number of months necessary to ensure such an orderly winding-down or restructuring of its clearing activities (the "winding-down period"). Such an estimation should include variety of business scenarios and might be quite difficult to calculate for a CCP, but EBA considers that there is no alternative to ensure the full application of Article 16(2) as it is written.

Furthermore, the CCP is required to provide more details demonstrating that the estimation of the winding-down period is sufficiently prudent in any cases.

1. In order to calculate the operational expenses referred to in Article 3, a CCP shall firstly calculate its ongoing annual expenses referred to in paragraph 2; secondly, divide the resulting number by twelve in order to determine its monthly operational expenses; and finally multiply the resulting number by its estimated winding-down or restructuring period. The estimation of the winding-down or restructuring period is subject to a floor of twelve months.

Explanatory text for consultation purposes

The estimation of the winding down or restructuring period should remain a CCP's responsibility. A CCP has to ensure that the duration of the winding-down or restructuring period is sufficient to ensure, including in stressed market conditions, an orderly winding-down or restructuring of its activities, reorganising its operations, liquidating its clearing portfolio or transferring its clearing activities to another CCP. In any case, the time span of the winding down or restructuring period that will be used for the calculation of the operational expenses is proposed to be subject to a floor of 12 months.

2. Ongoing annual gross expenses of a CCP are:

- (a) Staff costs, which are:
 - (i) Wages, salaries and other employee's remunerations(including variable remuneration)
 - (ii) Salaries charges and social insurance,
 - (iii) Other employee's expenses/staff costs.
- (b) External costs, which are expenses related to:
 - (i) Offices and building rents,
 - (ii) Software and equipment,
 - (iii) Communications,
 - (iv) Travelling, marketing and promotion,
 - (v) Professional services and outsourcing,
 - (vi) Information services,
 - (vii) Energy and heating,
 - (viii) Security, cleaning and maintenance,
 - (ix) Publications,
 - (x) Consulting services,
 - (xi) Legal services,
- (c) Taxes,
- (d) Losses related to operational failures,
- (e) Other expenses as defined in the applicable accounting framework.

The CCP shall also include additional costs that may occur in case of winding-down or restructuring its activities.

Article 7

Capital requirements for operational risk

Explanatory text for consultation purposes

The Basic Indicator Approach (BIA) is a valid starting point for the calculation of the capital requirements to cover operational risk. However, it is possible that the BIA understates the real risks for CCPs with low revenues (as in case of a start up CCP).

The Standardised Approach provided in the CRD framework for banks is not appropriate for CCPs since the business lines of such approach are not adapted to the activities carried out by CCPs.

CCPs should be allowed, subject to the same strict organisational and quantitative standards as for banks and to the permission of the competent authority, to use the AMA in order to incentivise them to increase their operational risk management. To ensure a proper capitalisation of operational risk, the CCPs using the AMA should respect a floor of 80% of the capital requirements calculated on the basis of BIA.

1. A CCP shall calculate its capital requirements for operational – including legal - risk referred to in Article 3 using either the basic indicator approach or advanced measurement approaches as provided in Regulation (EU) No xxxx/2012 of the European Parliament and of the Council of xx ... 2012 on prudential requirements for credit institutions and investment firms¹¹ subject to the restrictions provided in paragraphs 2 to 7.
2. A CCP may use the basic indicator approach in order to calculate its capital requirements for operational risk in accordance with Articles 304 to 305 of the Regulation (EU) No xxxx/2012.
3. A CCP shall have in place a well-documented assessment and management system for operational risk with clear responsibilities assigned for this system. It shall identify its exposures to operational risk and track relevant operational risk data, including material loss data. This system shall be subject to regular independent review carried out by an internal or external party possessing the necessary knowledge to carry out such review.
4. A CCP operational risk assessment system shall be closely integrated into the risk management processes of the CCP. Its output shall be an integral part of the process of monitoring and controlling the CCP's operational risk profile.
5. A CCP shall implement a system of reporting to senior management that provides operational risk reports to relevant functions within the institutions. A CCP shall have in place procedures for taking appropriate action according to the information within the reports to management.
6. A CCP may also apply to its competent authority for permission to use advanced measurement approaches. The competent authority may grant the CCP the permission to use advanced measurement approaches based on its own operational risk measurement systems, where all the qualitative and quantitative standards set out in Articles 310 and 311 of the Regulation (EU) No xxxx/2012 are met and where the CCP meets the general risk management standards set out in Articles 73 and 83 of the Directive (EU) No xxxx/2012 of the European Parliament and of the Council of xx ... 2012 on prudential requirements for credit institutions and investment firms¹². If the permission is granted by the competent authority, the CCP shall calculate its capital requirements for operational risk in accordance with Articles 310 to 313 of the Regulation (EU) No xxxx/2012.

¹¹ OJ...

¹² OJ...

7. CCPs using the Advanced Measurement Approaches as specified in paragraph 6 for the calculation of their capital requirements for operational risk shall provide capital which is at all times more than or equal to 80% of the capital required using the basic indicator approach according to paragraph 2.

Article 8

Capital requirements for credit, counterparty credit and market risks stemming from non-covered activities

Explanatory text for consultation purposes

EBA considers that such risk exposures stemming from non-covered activities should be calculated using some approaches set out for banks by the CRR.

Investment activities expose the CCPs at least to the same kind of credit risks that is typically faced by credit institutions. As the risk does not depend on the nature of the institutions but on the activities performed, it seems appropriate to refer to the prudential framework for banks but to take into account the concentration of risks stemming from derivatives that CCPs are exposed to.

In EBA's view, the CCPs should calculate its risk-weighted assets according to the Standardised Approach for credit risk. According to such method, the exposure value of an asset (i.e. its risk-weighted value) is equal to the product of its accounting value and the specific risk weight associated. The risk weights range from 0% for to 150%. Capital requirements for credit risks would be equal to the 8% of the risk-weighted assets.

EBA also considers that market risk, i.e. risk related to movements in markets factors, such as interest rates, should be calculated using the Standardised Approach for market risk set out for banks by the Capital Requirements Directive. According to such method, capital requirements for market risk are calculated using position risk adjustment factors applied to market values of the positions held by the CCP.

1. A CCP shall calculate its capital requirements for credit, counterparty credit and market risks stemming from its non-covered activities referred to in Article 3 as the sum of 8% of its risk-weighted exposure amounts for credit and counterparty credit risk and its capital requirements for market risk calculated in accordance with the Regulation (EU) No xxxx/2012, subject to the restrictions provided in paragraphs 2 to 5.
2. Investing its own financial resources as referred to in Article 47 of Regulation (EU) No xx/xxxx [EMIR], lending securities or commodities received as collateral, depositing cash collateral received, making repurchase transactions on collateral, borrowing transactions

or margin lending transactions shall be considered as non-covered activities carried out by a CCP.

3. For the calculation of capital requirements for market risk stemming from the non-covered activities it carries out, a CCP shall use the standardised approach for market risk provided for in Articles 315 to 350 of the Regulation (EU) No xxxx/2012.
4. For the calculation of the risk-weighted exposure amounts for credit risk stemming from the non-covered activities it carries out, a CCP shall apply the Standardised Approach for credit risk provided for in Articles 106 to 136 of the Regulation (EU) No xxxx/2012.
5. For the calculation of the risk-weighted exposure amounts for counterparty credit risk stemming from the non-covered activities it carries out, a CCP shall use the Mark-to-market Method provided for in Article 269 of the Regulation (EU) No xxxx/2012 for derivative transactions and the Financial Collateral Comprehensive Method applying supervisory volatility adjustments provided for in Articles 218 and 219 of the Regulation (EU) No xxxx/2012 for repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions.

Article 9

Capital requirements for business and legal risks

Explanatory text for consultation purposes

The risks faced by CCPs may differ in nature to those faced by banks, reflecting their different roles, and so applying only the bank regulatory framework may not capture them appropriately.

For the purposes of the review and evaluation referred to in Article 21 of Regulation (EU) No xx/xxxx [EMIR], the competent authority shall have the power to require a CCP to hold capital in excess of the capital requirements laid down in Article 3 or to decrease its exposure to risks if deemed necessary. The competent authority shall take into account legal risk not captured in Article 7 and business risk. Business risk refers to the risk a CCP assumes due to potential changes in general business conditions, such as market environment, client behaviour and technological progress.

Article 10

Monitoring and reporting

1. A CCP shall have procedures in place to identify all sources of risks that may impact its on-going functions and shall consider the likelihood of potential adverse effects on its revenues or expenses and its level of capital. A CCP shall monitor the compliance with the capital requirements set in Article 3 on an ongoing basis.

2. A CCP shall report the compliance with the capital requirements set in Article 3 to its competent authority on a quarterly basis.

Article 11

This Regulation shall enter into force 20 days after publication in the *Official Journal of the European Union*.

It shall apply 6 months after its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

*[For the Commission
The President]*

*[For the Commission
On behalf of the President]*

[Position]

V. Accompanying documents

a. Draft Impact Assessment

Introduction

The draft Regulatory Technical Standards (RTS) have to be accompanied with an impact assessment according to the Article 10(1) of the EBA Regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council).

Article 16 of the European Commission's (EC) proposals for a Regulation on over-the-counter (OTC) derivatives, central counterparties (CCPs) and trade repositories ('EMIR') requires the EBA to draft regulatory technical standards (RTS) on the capital requirements that a CCP should meet.

The EBA has had regard to the EC's Impact Assessment¹³ accompanying the EC's proposals for EMIR.

Procedural issues and consultation process

On March 6th 2012 the EBA published a Discussion Paper on this draft regulatory technical standard for consultation, including seeking data in order to conduct a cost benefit analysis.

The EBA received 21 comments, in particular from CCPs (9), banking and financial associations (5), banks (4), and other financial institutions (2). The EBA analysed these comments and considered them in drafting this RTS.

Scope and nature of the problem

As explained in the introduction of this consultation paper, the primary function of a CCP is to act as an intermediary between the counterparties to a bilateral trade, so that the parties' bilateral trade is replaced by each of them having a separate trade with the CCP. In this way, the CCP takes on the risk of the potential loss to which a party could be exposed if its counterpart were to default. Therefore, a CCP allows market participants to trade without being exposed to the risk of each other's default.

Given that the Regulation introduces a legal obligation to clear OTC derivatives transactions through CCPs thereby exposing CCPs to higher risks, it has to be ensured that these institutions are robustly risk-managed and financially sound irrespective of the financial instruments cleared.

To limit its credit exposures, the Regulation requires that a CCP collects margin, maintains a pre-funded default fund and maintains dedicated own re-

¹³ http://ec.europa.eu/internal_market/financial-markets/docs/derivatives/20100915_impact_assessment_en.pdf

sources. The CCP's dedicated own resources cannot be used to meet the CCP's regulatory capital requirements.

Further, additional capital is required under Article 16 of the Regulation to mitigate, against market risk, credit risk and counterparty credit risk arising from investment activities and other non-clearing activities; and also to mitigate against operational risk arising from all the activities of a CCP (including those covered and non-covered).

The EU Commission's Impact assessment of the EMIR

The EU Commission's Impact Assessment of the EMIR views the reduction of systemic risk is met by increasing the safety and efficiency of the OTC derivatives market as the general policy objective and sets the following specific policy objectives:

- a) To increase the transparency of the OTC derivatives market for regulators, market participants and the public;
- b) To reduce the counterparty credit risk associated with OTC derivatives; and
- c) To reduce the operational risk associated with OTC derivatives.

These goals are further broken down into the following operational objectives:

- a) To obtain complete and comprehensive information on OTC derivatives' positions;
- b) To increase the use of CCP clearing;
- c) To improve bilateral clearing practices; and
- d) To increase the standardisation of OTC derivatives contracts and processes.

This draft RTS tackles the operational objective b), "increase the use of CCP clearing" ensuring that the CCPs are prudently managed. The aim is to protect the CCPs themselves, the clearing members and their clients, by specifying rules that should ensure the continuation of the operations.

In particular, the draft RTS refers only to the activities not covered by specific financial resources since the covered activities are already subject of other technical standards.

Baseline scenario

Prior to this proposed Regulation, CCPs were not subject to EU CCP capital requirements. Although in some Member States, a CCP can have a banking licence and thereby be partially subject to the same regulation and capital requirements as a bank. For those other Member States, which do not subject a CCP to have a banking licence, the capital requirements are typically estimated following the CPSS-IOSCO principles using the operational expenses as proxy for the overall risk.

Article 16.2 of the EMIR defines the capital requirement for CCPs and requires the estimate of market, credit, counterparty credit, other risks and the operational expenses for an orderly wind-down or reorganisation of the operations.

The baseline scenario is the current status quo. The impact will be measured assuming that all the CCPs are subject to the capital requirements defined in Article 16 of the EMIR with the specification of the draft RTS.

An alternative baseline scenario could consider that the Regulation is implemented in the absence of the technical standard. In this case however, the Regulation does not specify how the risk measures should be estimated and would be impossible to have a quantitative assessment of the impact. For this reason, the baseline scenario is defined as in the previous paragraph.

Data used for the Impact Assessment

To gather data to assist the EBA in conducting its Impact Assessment several questions on the consequences of different policy options were asked in the Discussion Paper EBA/DP/2012/1.

Under various options, the CCPs were asked to estimate for the years 2007-2011:

- a) appropriate time span for winding down or restructuring a CCP's activities;
- b) capital requirements for operational risk;
- c) capital requirements for credit risk;
- d) capital requirements for counterparty credit risk;
- e) capital requirements for market risk.

At the time of publication of this Consultation Paper, the collection of these data is still in progress.

Likely economic impact

Capital requirements will be substantially higher than in the past, given that currently CCPs usually only compute the capital requirements using the approach based on operational expenses.

The proposed capital requirements will increase the soundness and robustness of CCPs, thereby helping to limit the costs for the society in case of a default of a CCP. The proposed requirements will also help improving the internal risk management processes of a CCP.

Further it is envisaged that the compliance costs for CCPs will rise due to the implementation of processes to calculate, monitor and report the capital requirements; including the possible need to develop IT systems, and increase compliance and IT staff.

Moreover, this cost will likely be larger for those CCPs that do not already compute the capital requirements using the approach based on operational expenses.

Further there will be a direct cost for supervisors:

- a) The supervisors will have to assess whether the CCPs meet all the requirements of these Technical Standards e.g. they have to assess the internal models for operational risk when required by a CCP, and they have to assess and monitor the capital plans submitted by the CCPs. At this juncture, EBA is not aware that there is a CCP currently using the Advance Model Approach to estimate the operational risk.
- b) Supervisors will also incur higher costs since they have to address business and legal risks as per Article 9 of the draft RTS.

Considered and preferred options

Options on Capital requirements

The EBA decided to retain the requirement that a CCP should hold capital including retained earnings and reserves that is at all times at least equal to the sum of the following two amounts:

- a) its operational expenses during an appropriate time span for winding-down or restructuring its activities;
- b) the sum of the capital requirements for the overall operational risk and for credit, counterparty and market risks stemming from non-covered activities.

An alternative approach is to consider only the higher of the two quantities. This option was considered to be in conflict with the Level 1 text.

Another alternative approach is to consider operational expenses only (allowing differentiated treatment depending on the CCPs' size and type of activities). This option was considered also to be in conflict with the Level 1 text that explicitly stipulates that both aspects (operational expenses and risks) have to be covered by the capital requirements.

Options on the estimation of the winding down or restructuring period

The EBA decided that the estimation of the appropriate time span for the winding-down or restructuring of their activities should remain the CCPs' responsibility.

Advantage: The estimation will enhance the understanding of the risk and of the business for CCPs and Supervisors.

Disadvantage: The estimation is highly dependent on the actual market conditions at the time of winding down and also on the reasons which lead to the necessity to wind down.

As a consequence of the previous paragraph, the introduction of a floor is necessary and it is fixed at 12 months.

The final impact assessment and the feedback report will be published after the consultation period.

b. Questions for consultation

- Q 1. Do you support this approach to capital requirements?
- Q 2. Do you have any other option to suggest that is not covered in this draft RTS?
- Q 3. Do you consider there to be any alternative approach which is more appropriate that would be consistent with Article 16 of the Regulation?
- Q 4. What is the incremental cost to your CCP for the implementation of this proposal?
- Q 5. What is the incremental benefit to your CCP for the implementation of this proposal?
- Q 6. What is the incremental cost for the supervisors for the implementation of this proposal?
- Q 7. What is the incremental benefit for the supervisors for the implementation of this proposal?
- Q 8. What is your view on the notification threshold? At which level should it be set?
- Q 9. In your view, in which case should restriction measures be taken by the competent authority once the notification threshold is breached?
- Q 10. Which criteria do you take into account for estimating the appropriate time span for orderly winding down or restructuring of the CCP's activities?
- Q 11. What is your estimation for the number of months necessary to ensure an orderly winding-down or restructuring of the CCP's activities?
- Q 12. What is the incremental cost or benefit to your CCP of this proposal assuming that the time span for winding down or restructuring a CCP's activities is 12 month?
- Q 13. How do you currently measure and capitalise for operational risk?
- Q 14. Do you think that the banking framework is the most appropriate method for calculating a CCP's capital requirements for operational risk? If not, which approach would be more suitable for a CCP?

- Q 15. Do you think that the Basic Indicator Approach set out for banks is appropriate for CCPs?
- Q 16. In your view, which alternative indicator should the EBA consider for the Basic Indicator Approach?
- Q 17. What would be the incremental cost of employing the basic indicator approach set out for banks for the calculation of your capital requirements for operational risk?
- Q 18. Do you think CCPs should be allowed to calculate the capital requirements for operational risk with an internal model, as in the advanced measurement approach?
- Q 19. Which other approaches should the EBA consider for operational risk measurement?
- Q 20. What are the incremental costs and benefits to your CCP for the implementation of the advanced measurement approach for operational risk?
- Q 21. Do you think CCPs should be allowed to calculate the capital requirements for market, credit and counterparty credit risks with internal models?
- Q 22. How do CCPs currently measure and capitalise for credit, counterparty credit and market risk stemming from non-covered activities?
- Q 23. Do you think that the banking framework is the most appropriate method of calculating a CCP's capital requirements for credit, counterparty credit and market risk stemming from non-covered activities?
- Q 24. What are the incremental costs or benefits to your CCP of this proposal assuming that for credit risk stemming from non-covered activities is computed with the approach required in Article 8?
- Q 25. What are the incremental costs or benefits to your CCP of this proposal assuming that for counterparty credit risk stemming from non-covered activities is computed with the approach required in Article 8?
- Q 26. What are the incremental costs or benefits to your CCP of this proposal assuming that for market risk stemming from non-covered activities is computed with the approach required in Article 8?
- Q 27. Do you think that CCPs, should be allowed to calculate their capital requirements for credit, counterparty credit and market risk using internal models?

- Q 28. In your view, which other approaches should the EBA consider for credit, counterparty credit and market risk measurement?
- Q 29. What other risks should be considered in Article 9?