 Regulatory Policy Committee	OPINION	
Impact Assessment (IA)	Loss Allocation rules for Central Counterparties	
Lead Department/Agency	HM Treasury	
Stage	Final	
Origin	Domestic	
IA Number	HMT 1303	
Date submitted to RPC	15/03/2013	
RPC Opinion date and reference	18/04/2013	RPC13-HMT-1734
Overall Assessment	GREEN	
<p>Overall comments on the robustness of the OITO assessment</p> <p>The impact assessment (IA) states that this proposal deals with ‘financial systemic risk’ and therefore is out of scope. On this point alone, the Committee has concluded – mostly due to its own consideration of the policy intentions – that the proposal is out of scope, and qualifies for a ‘GREEN’ assessment on the basis of paragraph 2.9.8. v. ‘Financial systemic risk’ of the Better Regulation Framework Manual.</p> <p>The quality of the evidence base presented in the IA however, is poor. The Department will need to address the Committee’s observations on the quality of the IA in order to make it fit for purpose.</p>		
<p>Overall quality of the analysis and evidence presented in the IA</p> <p><i>Demonstrating financial systemic risk:</i> The IA states that the proposals address a threat to wider financial stability, but the Department could have explained more clearly why this proposal is out of scope of the OITO Methodology. The IA would benefit from including a more detailed explanation why the proposal meets the criteria of paragraph 2.9.8. v. ‘Financial systemic risk’ of the Better Regulation Framework Manual.</p> <p><i>Evidence base:</i> The Department has provided monetised estimates of certain costs. However, the IA does not provide any information on what assumptions have been made, nor have the figures been evidenced in any way. The IA needs to provide an explanation of the provenance of these figures to make decision makers aware of how robust they are and at how they were arrived at. Without this information it is impossible for the Committee to comment on whether or not these figures are robust.</p> <p><i>Inconsistency of cost estimates used:</i> The summary sheet of the IA describes the Total Net Present Value (NPV) as £5.15 million, but the preferred option summary gives a best estimate of £7.2 million. The IA should make clear which of the two figures is correct.</p> <p><i>The role of clearing houses, its members, risk and exposure:</i> The IA does not explain clearly the role and function of clearing houses in relation to financial markets, participants and the risks to which that they are exposed in the event of the failure of the members of the clearing house to meet their financial obligations. The IA needs to explain more clearly what risks clearing houses – and their members – are exposed to.</p>		

Stakeholder response to consultation / views sought: The IA states that the Department "...sought the views of recognised clearing houses and their members in January 2013..." (paragraph 1). However, the IA does not reference the views expressed by these entities. The IA should summarise the views of clearing houses and their members on the different proposals and preferred option. In particular, the IA explains that a number of clearing houses were already establishing voluntary rules for loss allocation. The Department must set out clearly why an approach based on voluntary rules has not been considered as an alternative to regulation.

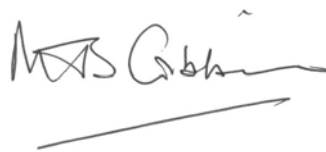
Benefits: The Department has not monetised any of the benefits in the IA. While full monetisation may not be possible the Department needs to at least attempt to demonstrate the scale of the potential benefits of the preferred policy option to allow decision makers to consider whether the benefits justify the costs.

EU minima: Although the cover sheet of the IA indicates that implementation of the proposal does not go beyond minimum EU requirements, the IA states that the "...Government intends to ensure that the policy change is consistent with the new European requirements on clearing houses to be introduced via EIMR [the European Market Information Regulation]. EMIR will bring in mandatory clearing obligations for OTC derivatives contracts and will set out a number of harmonised authorisation requirements which will result in all clearing houses having to apply for reauthorisation before they can provide clearing services. However, recital (50) of EMIR and Article 14(5) are clear that the requirements...do not prevent Member States from adopting or continuing to apply additional requirements in respect of clearing houses established in their jurisdiction" (paragraph 34). The Department should clarify to what extent the preferred option goes beyond the minimum requirements of the European Regulation. The IA should clearly identify and make clear any 'gold-plating' that is being introduced or retained in light of the EU Regulation.

European option: The IA discusses the potential impact of future EU related legislation that may come into force in the future – although the European Commission is currently consulting (paragraphs 35 to 37), the Department explains that it is not clear when formal proposals will be adopted. The IA would benefit from further discussion on how these domestically-generated proposals will be considered with such possible future EU legislation, or if the European Commission does not believe regulation is necessary in this area.

2009 prices: The IA uses a price base year of 2009. While the equivalent annual net cost to business (EANCB) figures are required to be in 2009 prices for the sake of consistency, it is normal to present the NPV in the appropriate price year for the policy, normally either the current year or the year when it is implemented. The IA should either use a more relevant price year or, to make the costs more transparent to decision makers, explain why 2009 has been used, especially as benefits have not been quantified.

Signed



Michael Gibbons, Chairman