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Review of incentives to clear OTC derivatives centrally

An evaluation of the post-implementation effects of reforms

The FSB and the other standard-setting bodies have agreed[1] to undertake an evaluation of the impact of G20 reforms on incentives to clear over-the-counter (OTC) derivatives centrally. This study to be undertaken by the Derivatives Assessment Team (DAT) will review the interaction of reforms affecting incentives for clearing. It will be carried out under the new FSB framework for post-implementation evaluation of effects of the G20 financial regulatory reforms (evaluation framework).[2] The final report will be completed in late 2018. The study follows an earlier review of the topic published in 2014.[3]

It is an appropriate time to re-examine whether adequate incentives to clear centrally are in place. Central clearing of standardised OTC derivatives was a key pillar of the G20 Leaders' commitments to reform OTC derivatives markets in response to the financial crisis. The key reforms relevant to incentives for central clearing have now been agreed and are being implemented. Central clearing rates have increased markedly since 2009, notably in interest rate derivatives and credit derivatives.[4]

However, concerns have been raised by some that the interaction of some post-crisis reforms may have contributed to inadequate incentives to clear centrally or may otherwise affect costs associated with providing clearing services or with accessing central clearing for some market participants, in ways that do not support the G20 Leaders' commitments. It would also be useful to understand how these incentives affect broader market functioning.

A number of post-crisis reforms have, or are expected to have, an impact on the incentives of market participants (including dealers and end users) to clear OTC derivatives through CCPs. Such reforms include:

- BCBS-IOSCO margin requirements for non-centrally cleared derivatives
- CPMI-IOSCO Principles for Financial Market Infrastructures
- Basel III framework aspects (including interim and final requirements for bank exposures to CCPs and to non-centrally cleared derivatives, Leverage Ratio and Liquidity Coverage Ratio)

Importantly, other national and regional policy differences, including exemptions and accounting and netting rules, may also affect the incentives to centrally clear.

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1 See FSB, *Chairs' Report on the Implementation of the Joint Workplan for Strengthening the Resilience, Recovery and Resolvability of Central Counterparties*, July 2017, www.fsb.org/wp-content/uploads/P050717-3.pdf

2 See FSB, *Framework for Post-Implementation Evaluation of the Effects of the G20 Financial Regulatory Reforms*, July 2017, at www.fsb.org/wp-content/uploads/P030717-4.pdf

3 See BIS, *Regulatory reform of over-the-counter derivatives: an assessment of incentives to clear centrally: A report by the OTC Derivatives Assessment Team, established by the OTC Derivatives Coordination Group*, October 2014, at www.bis.org/publ/othp21.pdf

4 See FSB, *Review of OTC derivatives market reforms: Effectiveness and broader effects of the reforms*, June 2017, at www.fsb.org/wp-content/uploads/P290617-1.pdf

The DAT study seeks to deliver a comprehensive assessment of whether the reforms are incentivising central clearing consistently with the G20 reform objectives across different asset classes/product types and for various classes of counterparty. It would also seek to take into account national and regional policy measures where these may be material to the overall structure of incentives. The DAT study's evaluation of the interaction of reforms will help inform any subsequent policy recommendations, bearing in mind the financial stability objectives of the reforms.

The assessment will be carried out by a specially constituted working group of approximately 25 representatives from a range of member authorities of the relevant standard-setting bodies. This working group will be responsible for developing the framework, consulting with industry representatives, conducting the analysis, writing the report and proposing any recommendations.