



Central Counterparties

For Prelims: Central Counterparties (CCPs), EMIR, ESMA

For Mains: CCP and how does it function in financial markets, implications of the ESMA's derecognition of Indian CCPs for European banks.

Why in News?

The **European Securities and Markets Authority (ESMA)**, the **European Union's** financial markets regulator, has **derecognized six Indian Central Counterparties (CCPs)** from April 30, 2023, in accordance with the **European Market Infrastructure Regulation (EMIR)**.

- These **six CCPs** are the Clearing Corporation of India (CCIL), Indian Clearing Corporation Ltd (ICCL), NSE Clearing Ltd (NSCCL), Multi Commodity Exchange Clearing (MCXCCL), India International Clearing Corporation (IFSC) Ltd (IICC) and NSE IFSC Clearing Corporation Ltd (NICCL).

What is CCP?

- **About:**
 - CCP is a financial institution that acts as an **intermediary between buyers and sellers in various derivatives and equities markets**. CCPs are structures that help facilitate the **clearing and settlement process** in financial markets.
 - The primary goal of CCPs is to increase efficiency and stability in financial markets.
 - CCPs reduce risks associated with **counterparty, operational, settlement, market, legal, and default issues**
 - CCPs act as a counterparty to both buyers and sellers in a trade, collecting money from each party involved and guaranteeing the terms of the trade
- **Functions:**
 - **Clearing and settlement** are the two main functions of a CCP.
 - Clearing involves **validating the details of the trade** and ensuring that both **parties have sufficient funds to complete the transaction**.
 - Settlement involves the **transfer of ownership of the asset** or security being traded from the seller to the buyer.
- **Regulators in India:**
 - The **Reserve Bank of India (RBI)** for CCPs clearing money market instruments and foreign exchange derivatives.
 - A CCP is authorized by the RBI to operate in India under the **Payment and Settlement Systems Act, 2007**.
 - The **Securities and Exchange Board of India (SEBI)** for CCPs clearing securities and commodity derivatives.

Why has ESMA Derecognized Indian CCPs?

- **Reason:**

- The ESMA derecognized Indian CCPs due to their failure to meet all EMIR requirements.
- The decision came due to **'no cooperation arrangements' between ESMA and Indian regulators** - the RBI, the SEBI and the [International Financial Services Centres Authority \(IFSCA\)](#).
 - While ESMA wants to supervise these six CCPs, Indian regulators are of the view that **since these domestic CCPs operate in India and not in the EU, these entities cannot be subjected to the ESMA regulations**. They feel that these six CCPs have robust risk management and there is no need for a foreign regulator to inspect them.
- **Impact:**
 - As of the date of application of the withdrawal decisions, these CCPs **will no longer be able to provide services to clearing members** and trading venues established in the EU.
 - The decision will **impact European banks in India** as they will either need as much as 50 times higher capital to carry out trades involving the Indian central counterparties or will have to unwind positions with the central counterparties over the next 6 to 9 months.

What is ESMA?

- **ESMA is an independent EU authority.**
- ESMA enhances the **protection of investors and promotes stable** and orderly financial markets.
- ESMA is the direct supervisor of specific financial entities such as credit rating agencies, securitization repositories, and trade repositories

What is EMIR?

- EMIR is an EU regulation adopted in August 2012
- It aims to **reduce systemic, counterparty, and operational risk in the OTC derivatives market**
- **It sets higher prudential standards for CCPs and trade repositories**
- EMIR enhances risk mitigation techniques for non-cleared derivatives
- It establishes a framework for the recognition and supervision of third-country CCPs

[Source: ET](#)

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