



ALMA MATER STUDIORUM
UNIVERSITÀ DI BOLOGNA

ARCHIVIO ISTITUZIONALE DELLA RICERCA

Alma Mater Studiorum Università di Bologna Archivio istituzionale della ricerca

Brexit and the political economy of euro-denominated clearing

This is the final peer-reviewed author's accepted manuscript (postprint) of the following publication:

Published Version:

Brexit and the political economy of euro-denominated clearing / James Scott; Quaglia Lucia. - In: REVIEW OF INTERNATIONAL POLITICAL ECONOMY. - ISSN 1466-4526. - ELETTRONICO. - 28:3(2021), pp. 505-527. [10.1080/09692290.2019.1699148]

Availability:

This version is available at: <https://hdl.handle.net/11585/854887> since: 2022-02-10

Published:

DOI: <http://doi.org/10.1080/09692290.2019.1699148>

Terms of use:

Some rights reserved. The terms and conditions for the reuse of this version of the manuscript are specified in the publishing policy. For all terms of use and more information see the publisher's website.

This item was downloaded from IRIS Università di Bologna (<https://cris.unibo.it/>).
When citing, please refer to the published version.

(Article begins on next page)

This is the final peer-reviewed accepted manuscript of:

Scott James, Lucia Quaglia (2021): Brexit and the political economy of euro-denominated clearing, *Review of International Political Economy* 28 (3): 505-527

The final published version is available online at:

<https://doi.org/10.1080/09692290.2019.1699148>

Terms of use:

Some rights reserved. The terms and conditions for the reuse of this version of the manuscript are specified in the publishing policy. For all terms of use and more information see the publisher's website.

This item was downloaded from IRIS Università di Bologna (<https://cris.unibo.it>)

When citing, please refer to the publisher version.

Brexit and the political economy of euro-denominated clearing

Scott James (King's College London)

Lucia Quaglia (University of Bologna)

Abstract

The decision by the United Kingdom (UK) to withdraw from the European Union (EU) has reignited tensions around the clearing of euro-denominated derivatives. Yet, the EU has resisted concerted pressure from several member states and the ECB to force the relocation of euro clearing away from London. Instead, it has opted to strengthen the supervision of EU and non-EU Central Counterparties (CCPs), leaving the derecognition of third-country CCPs as a last resort. How do we explain this? This article adopts a synthesis approach, combining theories with distinct domains of application to provide a more comprehensive explanation. We argue that a state-centric perspective helps us to understand the preferences of key member states, but it cannot fully explain the EU's position because it ignores the critical role of supranational institutions. In addition, a transnational approach has limited explanatory power because the most concerted opposition came from a small number of dealer banks, not a wide coalition of financial interests. To address these gaps, we argue that incorporating a bureaucratic politics perspective can add significant analytical leverage. This reveals that the EU's resistance to a location policy reflected the need to reconcile the competing bureaucratic interests of different supranational institutions.

INTRODUCTION

The decision by the United Kingdom (UK) to withdraw from the European Union (EU) has reignited tensions concerning the clearing of euro-denominated instruments – principally derivatives – which emerged at the height of the sovereign debt crisis in the euro area. Clearing is the process by which a ‘clearing house’, also called a ‘central counter party’ (CCP), acts as the middleman for both the buyer and the seller of a financial instrument. Clearing is important for financial stability given the huge volume of trades in derivatives and securities that are conducted daily. But it is also a lucrative financial activity for those financial centres capable of attracting this business. Given that the bulk of euro-denominated clearing takes place in London, EU rules governing the recognition and supervision of CCPs have important implications for the functioning of derivatives markets worldwide.

At the height of the euro area sovereign debt crisis in July 2011, the ECB issued a policy paper calling for CCPs that cleared a significant proportion of euro-denominated financial instruments to be located in the euro area (ECB 2011). The proposal was strongly opposed by UK policy-makers, keen to retain the profitable euro clearing business in the City of London. Although the UK government successfully challenged the ECB’s plans in the European Court of Justice (ECJ), efforts to revive the so-called ‘location policy’ for euro clearing gathered pace following the Brexit vote in June 2016. This led to repeated calls from French and German politicians, together with senior ECB officials, for London to lose its pre-eminent status in the clearing of euro-denominated instruments (Fouquet and Detrixhe 2016).

Despite this, the EU has resisted pressure to force the relocation of euro clearing. The legislative proposal put forward by the European Commission in June 2017, and agreed by

the Council of Ministers and the European Parliament in March 2019, did not seek to reinstate an automatic relocation requirement for CCPs conducting euro clearing above a certain threshold, as originally envisaged by the ECB. Instead, the revised European Market Infrastructure Regulation (known as EMIR II) called for the strengthened supervision of both EU and non-EU CCPs through the creation of a new supervisory mechanism within the European Securities and Markets Authority (ESMA). EMIR II also proposed a new ‘two-tier’ system for classifying third-country CCPs (which, it was envisaged, would include the UK) whereby ‘systemically important’ CCPs would be subject to stricter regulatory requirements and strengthened EU-level supervision. Importantly, if the requirements were insufficient to mitigate the potential risks, then CCPs deemed ‘substantially systemically important’ could be derecognised and only authorised to provide services to EU customers if they were (re)located in the EU.¹ However, important safeguards were inserted into the text so that derecognition of a third-country CCP would only happen as a ‘last resort’, and should in practice never be needed (interviews, London, Brussels, September 2018).

The EU’s resistance to introducing a strict location policy for euro clearing is puzzling both empirically and theoretically. Euro clearing has significant implications for financial stability across the EU, and the effectiveness of monetary policy within the euro area. It is also an important source of tax revenue and employment for those financial jurisdictions in which a large volume of trades are cleared. We would, therefore, expect the main EU authorities (particularly, the Commission, the ECB, and ESMA) to push strongly for the relocation of euro clearing to the EU after Brexit. Member states with large financial centres (notably, France, Germany and Italy), together with their established CCPs, also stood to gain considerably from greater third country restrictions. We would, therefore, expect them to

exploit the window of opportunity provided by Brexit in order to ‘repatriate’ euro clearing. How, then, can we explain the new EU legislation on euro clearing?

We draw on different theoretical approaches in political economy to shed light on this puzzle. First, we argue that state-centric approaches (Donnelly 2014; Drezner 2007; Knaack 2015; Helleiner 2014; Rixen 2013, 2010), rooted in varieties of financial capitalism (Fioretos 2011, 2010; Goldbach 2015a,b; Howarth and Quaglia 2016; Lavery et al 2018; Macartney 2010), and historical institutionalism (Büthe and Mattli 2011; Thiemann 2014, 2018), do a good job of explaining the concerted push by French and German policy-makers, and their respective financial centres, to adopt euro clearing restrictions. They also account for why the UK and the US policy-makers, allied with their national financial industries, sought to resist euro clearing restrictions. In practice, however, US and UK regulators had divergent preferences on crucial aspects of CCP regulation, and their efforts to lobby against the changes were viewed as ineffectual. State-centric approaches, therefore, struggle to explain why the EU chose to resist Franco-German pressure to relocate euro clearing.

Second, transnational perspectives that emphasise interdependence (Farrell and Newman 2014; Newman and Posner 2018), mutual interests (Cerny 2010; McKeen-Edwards and Porter 2013; Mügge 2010; Porter 2014; cf Young 2012) and shared norms (Tsingou 2015; Seabrooke and Wigan 2016) also have significant limitations. On the one hand, quiet opposition did come from a small number of French and German ‘dealer’ banks, responsible for the bulk of trading in derivatives, which lobbied the Commission and Parliament against the increased costs of market fragmentation. On the other hand, however, EU-based CCPs (notably, those in France, Germany and Italy) strongly favoured relocation as they were well placed to attract business away from London, while financial and non-financial end-users of

derivatives were weakly organised. We, therefore, find little evidence of a powerful transnational coalition of financial interests mobilised around euro clearing. Hence, state-centric and transnational accounts provide only a partial – and potentially misleading – explanation of the EU’s position on euro clearing.

To provide a more comprehensive explanation of the EU’s policy on euro clearing, we argue that it is necessary to incorporate theories of bureaucratic politics which emphasise the agency of supranational institutions (Bach et al. 2016; Busuioc 2016; Carpenter 2001; Egeberg and Trondal 2011; Trondal et al 2013). This paper suggests that the EU’s cautious approach was shaped in large part by bureaucratic competition and rivalry between the Commission, the ECB and ESMA, as well as national regulators, over the location and supervision of CCPs. In particular, the outcome of EMIR II reflected the need to reconcile divergent bureaucratic interests and policy preferences, including: the Commission’s concern with the integrity of the single market, the costs of restricting euro clearing, and the desire to strengthen the EU’s third country equivalence regime; the ECB’s support for relocation to the euro area on financial stability grounds and the demand for greater powers of oversight over clearing; and the concerted push by ESMA to increase its powers by centralising supervision of EU and non-EU CCPs. It was the need to balance these competing bureaucratic interests that explains why the EU resisted pressure to propose a strict location policy.

The article makes two main contributions to the literature. Empirically, we add to a growing corpus of post-crisis literature on the international political economy of derivatives regulation (Helleiner et al. 2018; Helleiner 2014; Gabor 2016; Knaack 2015), ongoing transatlantic disputes in financial regulation (Farrell and Newman 2014; Newman and Posner 2018; Pagliari 2013) and the political economy of Brexit (see, for example, the special issues of

New Political Economy 2018, *Journal of European Public Policy* 2018; Lavery et al. 2018).

In particular, this article focuses on the under-explored issue of euro-denominated clearing which has received relatively little attention from political economists (except for Friedrich and Thiemann 2018). Theoretically, the article highlights the advantages of adopting a synthesis approach (Jupille et al 2003: 21), which integrates theories with distinct domains of application to provide a more comprehensive explanation of the empirical world. As such, we assess the explanatory power of mainstream political economy approaches, highlighting the gaps in our understanding that these generate. Next, we showcase the value-added of incorporating a bureaucratic politics perspective which directs our attention to the power and preferences of important supranational institutions.

The argument is developed as follows. Section 2 outlines the market structure and the main issues concerning euro clearing. Section 3 reviews the literature on the political economy of finance and the politics of financial regulation, teasing out theoretical insights that can be applied to euro clearing. Sections 4 and 5 assess the explanatory power of different theoretical approaches against the empirical record through the method of process-tracing. Section 6 concludes. The empirical material was gathered through a systematic survey of press coverage, and seventeen anonymised interviews conducted with regulators, industry stakeholders and elected officials based in Brussels, Paris, London, Frankfurt and Washington.

2. CLEARING OF EURO-DENOMINATED TRANSACTIONS: MARKET AND REGULATORY ISSUES

Contracts cleared by CCPs can be securities (bonds or equities), securities financing transactions (including repurchase agreements, i.e. repos) or financial derivatives, whether listed or over the counter (OTC), that to say, traded bilaterally. In 2017, approximately 90% of all derivatives were OTC derivatives; around 60% of all OTC derivatives were centrally cleared through CCPs; and about 97% of all centrally-cleared derivatives contracts were interest-rate derivatives (swaps) (Commission 2017a). The repo market, albeit smaller, is also important because repos are used by central banks as instruments of monetary policy and they have implications for the costs of (re)financing the public debt (sovereign bonds) (Gabor 2016).

The main players in the clearing business are: dealers, CCPs and end-users within and without the financial sector. The main traders of OTC derivatives are ‘dealer banks’, the most important being a group of sixteen large banks based in the US, the UK, France, Germany and Japan, whose views tend to be represented by the International Swaps and Derivatives Association (ISDA) (Newman and Bach 2014).² The main CCPs worldwide are the London Clearing House (LCH) in the UK, and the Depository Trust & Clearing Corporation (DTCC), the Chicago Mercantile Exchange (CME), the Intercontinental Exchange Clear (ICE), which are all based in the US, but also operate with subsidiaries in the UK. Collectively, these CCPs account for most of the cleared activity globally. In the UK, LCH Clearnet is the main clearing house for interest rates derivatives worldwide: it clears swaps in 18 currencies for customers in 55 jurisdictions, including (daily) approximately \$2 trillion in US dollar-denominated contracts, and \$1 trillion in euro-denominated contracts. The clearing of dollar swaps is governed by special supervisory arrangements agreed between US and UK regulators.

The regulatory reforms enacted after the international financial crisis enhanced the role of CCPs with a view to protecting financial stability (for an overview, see Helleiner et al. 2018). The fact that the market for central clearing is concentrated - a few CCPs offer the bulk of clearing services, especially in certain asset classes - poses two regulatory challenges. On the one hand, global CCPs provide cheaper services to their customers because of the netting of transactions that take place within the CCPs, often across various currencies (e.g. Carney 2017; Rolet 2016; ICE 2016). On the other hand, global CCPs concentrate financial risk, hence their failure could threaten financial stability (e.g. Mersch 2017; Tucker 2011; Commission 2017a). Of particular concern is a situation whereby the bulk of clearing of transactions in a given currency takes place outside the jurisdiction which issues that currency.

The City of London's position, outside the euro area and (after Brexit) outside the EU, poses a profound challenge. The failure of a global CCP based in the UK could have huge negative implications for financial stability in the EU, given that approximately 90% of euro-denominated transactions are cleared in London (Coeure 2017; Mersch 2017; Commission 2017a). Moreover, the clearing of the repo market in London affects the transmission mechanism of ECB monetary policy, while the operations of UK-based CCPs can also have detrimental effects on euro area sovereign debt. Indeed, in 2011 policy-makers in several member states claimed that LCH aggravated the sovereign debt crisis by raising its margin requirements — the amount that market participants need to post as collateral — on the debt for Spain and Italy (Stafford 2017; interview, Brussels, May 2018). On the basis of these arguments, many prominent voices called for the bulk of euro clearing to be located within the EU, ideally in the euro area, and for the supervision of EU authorities to extend to non-EU CCPs that engage in substantial amounts of euro clearing.

Opponents pointed out that a location policy, such as this, would fragment the derivatives market, resulting in higher costs for end-users. This was because removing euro-denominated transactions from large netting agreements in London would lead to smaller netting agreements across separate CCPs, thereby requiring end-users to post higher margin collaterals. For example, the chairman of the London Stock Exchange (LSE) (Rolet 2016) claimed that the disaggregation of the euro component of the clearing engine would impose massive costs on the financial industry through higher margin requirements (see also ICE 2016). There is no specific data available concerning the value of euro clearing to the UK. However, a report by Oliver Wyman (2016, p. 4), commissioned by The CityUK, estimated annual revenues from clearing to be £3-4 billion and annual tax contributions of £1-3 billion. A report conducted by Ernst and Young in 2017 claimed that up to 83,000 clearing jobs could be lost in London ‘in a worst case scenario’ (Hope 2017). The wider impact on the financial ecosystem of relocating euro clearing could, therefore, be substantial. For this reason, US and UK policy-makers and industry leaders strongly argued against the imposition of new euro clearing restrictions.

3. THEORETICAL APPROACHES TO THE POLITICAL ECONOMY OF EURO CLEARING

Several bodies of work in political economy can be useful in understanding the regulation of euro clearing. The first provides a state-centric perspective (Büthe and Mattli 2011; Donnelly 2014; Drezner 2007; Fioretos 2011, 2010; Goldbach 2015a,b; Howarth and Quaglia 2016; Macartney 2010; Rixen 2013, 2010; Thiemann 2014, 2018). It focuses on the institutional configuration of national economic systems, arguing that national policy-makers seek to

defend the comparative institutional advantages of their domestic financial industry. This ‘economic patriotism’ (see Clift and Woll 2012; Rosamond 2012) or ‘neo-mercantilism’ (Howarth and Quaglia 2018) predicts fierce competition amongst jurisdictions to attract lucrative financial activity, such as euro clearing (on US-EU competition for derivatives trading, see Knaack 2015 and Helleiner 2014).

A second approach draws on the transnational governance literature (Djelic and Quack 2010) by highlighting the critical role of large transnational financial groups (Graz and Noelke 2008; McKeen-Edwards and Porter 2013; Mügge 2010), transgovernmental networks of regulators (Tsingou 2015; Porter 2014), and professional networks (Seabrooke and Henriksen 2017; Seabrooke and Wigan 2016). According to Cerny’s ‘transnational neopluralism’ (2010: 4-6), the most important ‘movers and shakers’ are no longer domestic forces, but rather ‘actors that can coordinate their activities across borders’. Similarly, the ‘new interdependence’ approach (Farrell and Newman 2016, 2014; Newman and Posner 2016, 2018) examines the formation of cross-border coalitions brought together by mutual interdependence. All these works pay attention to the mobilisation of transnational networks (coalitions) of private and public actors, which act as a powerful force in defence of cross-border financial activity and the promotion of transnational financial regulation. For example, these coalitions have been instrumental in settling transatlantic regulatory disputes concerning accounting standards (Farrell and Newman 2015) and derivatives (Newman and Posner 2018).

The limitation of these two political economy perspectives is that they actually say relatively little about the critical role or importance of supranational institutions. From both perspectives, the EU institutions have limited agency: rather, their preferences and actions are

largely ascribed to power dynamics and intergovernmental bargaining between national governments, or to capture by organised transnational economic interests. But this is to significantly downplay the agenda-setting and policy-making capacities of EU supranational institutions in the realm of financial regulation and macroeconomic policies (see Epstein and Rhodes 2016; Jabko 2006; Posner 2009, 2010; Verdun 2017). In particular, although political economy explanations provide a convincing account of the economic incentives held by key member states and financial sector actors, how these positions interact with the preferences of political and bureaucratic institutions is less clearly defined. This potentially leads to under-determined empirical predictions about the location and/or restriction of euro clearing, and the allocation of supervisory competence over CCPs.

To address this, we draw on the bureaucratic politics literature which focuses on the institutional interests and preferences of regulatory agencies (Carpenter 2001; Krause and Meier 2003; Peters 2002). This offers two key insights. First, it suggests that bureaucrats are highly protective of their particular bureaucratic ‘turf’, defined as an agency’s distinctive ‘jurisdiction’ (Wilson 1989: 185-88) or ‘regulatory domain’ (Maor 2010: 136). Bureaucrats will also seek to expand their ‘turf’ over time by increasing their budget, expanding their policy tasks and functions, and/or enhancing the status and quality of their work (Dunleavy 1991: 203-4). Second, bureaucrats are not impartial implementers of decisions made by elected officials. Rather, they have their own policy preferences, goals and ideological principles, which they seek to advance by shaping the policy agenda (Adolph 2013: 11). These characteristics frequently bring them into rivalry with other bureaucratic agencies with whom they are in competition for new policy competences, resources and influence (Baldwin et al 2011: 368).

The application of theories of bureaucratic politics at the transnational and supranational levels has grown significantly in recent years (see Bach et al 2016; Stone and Ladi 2015; Trondal et al. 2013), especially with reference to the EU. The extent of bureaucratic competition in the EU is compounded by multi-level structures, horizontal regulatory ‘networks’ (Coen and Thatcher 2008; Eberlein and Newman 2008), and agencies (Egeberg and Trondal 2011) with fluid (and often overlapping) policy mandates and delegated competences (Busuioc 2016: 41). After the financial crisis, three European Supervisory Agencies (ESAs) were established in the EU and were later joined by the Single Supervisory Mechanism (SSM) at the ECB.

The following sections assess the explanatory power of these distinct theoretical approaches against the empirical record. To provide a better understanding of euro clearing, we adopt a ‘synthesis’ approach which strives to combine theories with distinct domains of application to provide a more comprehensive explanation of the empirical world (Jupille et al 2003: 21-2). To be precise, this approach works by 1) identifying the respective turfs or ‘home domains’ of each theory; 2) specifying the causal claims of each theory independently; and 3) integrating these to produce an additive explanation. The aim is, therefore ‘to build a more comprehensive composite, in which the whole provides some gains over partial representations, all the while preserving the integrity of the contribution of the parts’ (ibid: 19).

The synthesis approach reveals that while state-centric and transnational perspectives have some explanatory leverage, both theories are characterised by an important analytical blind spot. Specifically, they say relatively little about the independent agency of supranational institutions, leading them to make under-determined predictions about the EU’s policy on

euro clearing. Integrating political economy explanations with a bureaucratic politics perspective reveals that the EU's cautiousness on euro clearing cannot be reduced to member state competition or transnational lobbying. Rather, it was rooted in the internal bureaucratic politics of the EU's supranational institutions, each of which was in competition to expand their policy competences in this area. Hence, we show that the influence of key member states, as well as parts of the financial industry, was in large part contingent upon the policy preferences of, and power dynamics between, the main EU institutions. We conclude that greater attention to the inter-institutional politics of the EU is therefore additive to existing political economy explanations, and enables greater specificity of the 'scope' conditions that define state-centric and transnational approaches.

4. EURO CLEARING AND THE 2011 ECB LOCATION POLICY

In February 2009, a (confidential) report compiled by a French working group headed by the Banque de France and including several representatives of the financial industry concluded that clearing was of strategic importance to the euro area and to Paris.³ The report outlined a possible set of actions, including the proposal for restricting the clearing of euro-denominated transactions to the euro area, urging the French authorities to campaign to this end. The document also suggested that the ECB should promote the establishment of CCPs in the euro area for reasons of financial and monetary stability. The report was prepared for the Haut Comité de Place, a body formed by French finance minister, Cristine Lagarde, to promote Paris's position in the financial markets. Later in the same month, Minister Lagarde mentioned the need for clearing euro-denominated financial products in the euro area, a position supported by the Governor of the Bank of France (Grant 2009). Although these arguments were justified in terms of financial stability, French policy-makers and market

players did little to disguise their longer-term goal of attracting euro clearing business to Paris.

In July 2011, the ECB issued a policy paper that called for legislation requiring CCPs to be based in the euro area if they handled ‘sizeable amounts’ (specifically, more than 5 per cent of the clearer’s total business) of a euro-denominated financial product (ECB 2011). This recommendation came in the context of a long-standing debate over the authorisation and supervision of CCPs in the European Markets Infrastructure Regulation (EMIR), on which the UK government had won an important concession, prohibiting discrimination against any member state as a venue for clearing services (Howarth and Quaglia 2017). The ECB’s primary motivation for proposing a ‘location policy’ was concern about financial stability, which was part of the ECB’s mandate. As one interviewee (London, May 2018) put it: ‘Some at the ECB genuinely believe that there are financial stability reasons for relocation. They are not willing to defer to foreign regulators that do not have much skin in the game, in the same way the ECB does.’ Yet, the location policy was also driven by bureaucratic politics: the ECB set out to expand its policy competences so as to include responsibility for the oversight of clearing, which was not explicitly within its remit. At the height of the euro area crisis, this was widely viewed as a ‘power grab...the ECB made a deliberate play for it...because they were on the back foot’ (interview, London, September 2018) to counter the growing influence of the ESAs by making the ECB a ‘regulatory superpower’ (interview, Frankfurt, August 2018).

In accordance with a state-centric explanation, UK policy-makers firmly opposed the ECB’s actions as it threatened the position of the City of London and its dominance of the lucrative euro clearing business. In September 2011, the UK government launched its first lawsuit

before the ECJ on the grounds that the ECB's location policy would restrict the free movement of capital and infringe the right of establishment in the Single Market. The financial industry, especially derivatives dealers, clearers and end-users (as well as the main industry associations, such as the ISDA and the FIA), was strongly supportive of the UK's legal challenge. However, contrary to what we would expect from a transnational explanation, there is little evidence that a powerful cross-border coalition of financial firms mobilised around the issue. Instead, industry concluded that with the reputation of the sector badly damaged, the 'UK government was de facto fighting this battle' and 'would be more effective than the industry in doing so' (interviews, London, June 2018).

After a four-year battle, the ECJ eventually ruled in the UK's favour. Importantly, however, this was on relatively narrow legal grounds that the ECB did not have the necessary competence to regulate clearing systems (ECJ Case T-496/11). Following the judgment, the ECB and the Bank of England agreed additional measures to manage the cross-border systemic risk implications of EU CCPs. This included strengthened information exchange and cooperation for UK CCPs with significant euro-denominated business, and the extension of existing swap lines to facilitate the provision of multi-currency liquidity support to CCPs by both central banks (ECB 2015). However, this exercise in transgovernmental regulatory cooperation proved short-lived as the issue was reignited just twelve months later.

5. BREXIT AND THE BATTLE OVER EURO CLEARING

Following the UK's decision to leave the EU in June 2016, calls for new restrictions on London's dominant role in euro clearing (re)gained momentum. The French government, strongly backed by the Paris-based financial industry and confident that they would be

supported by the ECB, were pivotal in forcing the question of euro clearing back onto the EU agenda. The French finance ministry spent six months prior to the UK referendum planning ‘what they wanted to go after’ in the event of a Leave vote and euro clearing was identified as a key priority (interview, London, September 2018). This was backed by the French financial regulatory authority, the *Autorité des Marchés Financiers*, which openly called for a new location policy not only for CCPs, but also for trade repositories (AMF 2017). Hence, the day after the referendum, the French President, François Hollande, announced that ‘the City, which thanks to the EU was able to handle clearing operations for the eurozone, will no longer be able to do them’ (Fouquet and Detrixhe 2016).

The German government initially refused to take a position on euro clearing, not least because regulators in the financial supervisory agency, the *Bafin*, cautioned against the complexity and risk of supervising large CCPs (interviews, Brussels, April and May 2018). Following the Brexit referendum, however, they came under increasing pressure from the French to support a location policy, and were ‘publicly shamed’ by *Deutsche Börse* for not doing more to promote Frankfurt as a financial centre (interview, London, September 2018). At the end of 2016, the German finance minister, Wolfgang Schäuble, changed tack and declared that euro clearing should be done within the euro area (Wagstyl and Chazan 2016), a position that was later reiterated by Andreas Dombret (2017), a member of the *Bundesbank* Executive Board. In July 2017, Frankfurt Finance and Paris Europlace (2017) issued a joint statement stressing the importance of operating the clearing of euro-denominated derivatives within the jurisdiction of the ECJ. Frankfurt, in particular, stood to benefit significantly from new clearing restrictions because *Eurex*, the CCP owned by *Deutsche Börse*, was the only EU CCP able to take on a substantial share of euro clearing. Further support for forced relocation also came from the largest clearing house in Rome, *Cassa di Compensazione e Garanzia*, and

the Bank of Italy (Canepa and Koranyi 2017). The state-centric, neo-mercantilist perspective, therefore, does a good job of explaining the French-led push to revive the ECB's location policy following Brexit to attract clearing business away from the UK, as well as the support of Germany and Italy.

Under pressure to repatriate euro clearing, the Commission agreed to reopen the issue. It did so by expanding the existing technical review of EMIR, which had been underway since 2015, to include the sensitive issue of CCP supervision. The French and German finance ministries regarded third country supervision as a 'trojan horse' for relocation and were 'very closely involved' in the drafting of the proposal, whereas the UK was largely excluded (interview, Brussels, August 2018). Despite this, the legislative proposal which emerged in June 2017, known as EMIR II, fell significantly short of the ECB's original location policy. Instead, it envisaged a new 'tiered' system for non-EU CCPs. 'Non-systemically important' third country CCPs would continue to provide their services under the EU's existing equivalence framework.⁴ However, 'systemically important' CCPs would be subject to stricter requirements, including full compliance with EMIR rules and additional requirements set by the relevant EU central banks, as well as agreement to provide ESMA with relevant information and to enable on-site inspections.

Importantly, non-EU CCPs could be designated as 'substantially systemically important' if the additional requirements outlined above were deemed insufficient to mitigate potential risks. In this instance, the Commission could decide that a CCP would only be able to continue providing services to EU clients if it established itself within the EU. The legislation specified that the criteria for assessing whether a third-country CCP was systemically important would be defined by the Commission, in cooperation with ESMA and the ECB

(Commission 2017a). This would include an assessment of a CCP's business (for example, the size and amount of euro clearing), its links to the EU (such as how many clearing members were EU entities), and the potential impact if such a CCP were to fail. ESMA would make a determination on whether a clearing house was systemically or substantially-systemically important, with input from the ECB, and the Commission would decide what action to take. The draft legislation therefore left open the possibility of requiring CCPs to relocate euro clearing to the EU, but granted the Commission considerable discretion over whether to do so. This discretion provided two critical safeguards: first, relocation would only occur in 'extreme circumstances' at the end of a 'very lengthy process'; and second, it ensured that the final decision was ultimately a 'political' one, rather than an 'automatic' or 'technical' one (interviews, Brussels and Paris, July and August 2018).

A bureaucratic politics perspective explains the EU's reluctance to propose a simple relocation policy in EMIR II as a consequence of having to balance the competing bureaucratic interests and preferences of the main supranational institutions. This bureaucratic battle had two dimensions: the first concerned the issue of relocation, the chief protagonists for which were the ECB and the Commission; and the second related to the issue of supervision, involving the ECB and ESMA. With respect to the first dimension, the ECB Executive Board remained supportive of the forced relocation of euro-denominated clearing to the euro area on financial stability grounds (Canepa and Koranyi 2017). Brexit heightened the ECB's concerns about the euro area's dependency on London for clearing derivatives, and regarded the Commission's proposal to be a significant 'rowing back' on its 2011 relocation policy (interview, Frankfurt, August 2018). It made little secret of its desire to see euro clearing relocated to the euro area, especially to Frankfurt, and successfully applied pressure on German banks, notably Deutsche Bank, to do so (interview, London, September

2018; see also Storbeck 2018). For this reason, the ECB was deeply concerned about the draft legislation. The prospect of the Commission (and ESMA) determining the fate of euro clearing ‘sent the ECB into a fit’ as this was viewed as a deliberate attempt to ‘try to push central banks out’ (interview, Frankfurt, August 2018).

By contrast, the Commission ‘has never wanted relocation and felt that it should always be the last resort’ (interview, London, September 2018). Back in 2011, for example, the Commission did not transpose the ECB’s location policy into legislation, and refused to support it when it was challenged in the ECJ, because relocation was viewed as discriminatory against non-euro area member states and thus illegal under EU law (interviews, Brussels, August and September 2018). Although this obstacle does not apply to third countries, the Commission refused to endorse an automatic relocation policy in 2017 on the grounds that this would impose huge logistical costs on EU banks. It also feared that clearing restrictions would be highly disruptive to financial markets, not least because the EU27 lacks the infrastructure to take over London’s clearing role.

But the Commission's opposition to a strict location policy was also motivated by bureaucratic politics in two key respects. First, the Commission sought to defend the interests of the EU institutions and the integrity of the single market. Although EMIR II only envisaged euro clearing being relocated to the EU27 (post-Brexit), the Commission shared the concerns of non-euro area states (notably, Sweden and Poland) that in practice relocation could discriminate against their clearing houses. In particular, they feared that the ECB would attempt to revive ‘the old location policy under a more complex guise’: namely, by using derecognition to quietly push for euro clearing to gravitate to the euro area on monetary policy grounds (interviews, Brussels and Paris, May and July 2018). Second, the Commission

viewed relocation as a ‘distraction’ from strengthening the EU’s third country equivalence regime for financial regulation more broadly – a process in which it played the lead role (interview, Brussels, August 2018). In fact, equivalence decisions are generally taken by the Commission, following the technical advice of the European Supervisory Authorities, such as ESMA. In some cases, all technical work is done by the Commission, with the assistance of external consultants. The Commission was also eager for the EU to gain regulatory and supervisory powers equal to the US authorities: as a senior official noted ‘they just want to be taken seriously...rather than being dismissed by central bankers and national regulators’ (interview, London, September 2018).

The second dimension of bureaucratic politics related to the supervision of CCPs. To ensure that the ECB would retain a ‘seat at the table’ in decision making over euro clearing, it pushed for greater powers of oversight for both EU and non-EU CCPs (interview, Brussels, June 2018). Senior figures argued that the ECB should be empowered to provide macroprudential oversight of CCPs to support its monetary policy and financial stability objectives. For example, ECB Executive Board Member Yves Mersch (2017) urged the Commission ‘to strengthen the role played by the central banks of issue of the EU in the regulatory framework...centred on the aspects of CCP risk management that are most essential for the fulfilment of their monetary policy mandates’. To support a strengthened oversight role, and to overcome the ECJ’s legal objections, in June 2017, the ECB proposed an amendment to article 22 of its statute so as to be granted the legal competence to regulate central clearing (interview, Frankfurt, August 2018). The change proposed by the ECB called for an ‘enhanced role for central banks of issue in the supervisory system of CCPs, in particular with regard to the recognition and supervision of systemically important third-country CCPs clearing significant amounts of euro-denominated transactions’ (ECB 2017). In

addition, the ECB recommended that it should be granted new regulatory powers ‘outside the framework of the Regulation...to adopt additional requirements for CCPs’ clearing significant amounts of euro-denominated transactions, to protect the stability of the euro (ECB 2019).

The ECB’s proposal was widely interpreted as a ‘power play’: the central bank wanted to ensure that in determining whether to impose new restrictions on euro clearing, the Commission would ‘not have to rely only on ESMA’, which the ECB regarded as lacking a ‘deep understanding’ of derivatives markets (interview, Brussels, June 2018). Yet, as one policy-maker commented ‘The ECB perspective of what it needs and would like is not shared by other institutions’ (interview, Brussels, September 2018). Thus, the Commission, the European Parliament and the Council of Ministers endorsed the ECB’s proposal, but subject to significant limitations: while the ECB would be conferred with an exhaustive list of new powers over non-EU CCPs, these would not be extended to EU CCPs.⁵ In protest, the ECB withdrew its request for a revision to Article 22 in March 2019, claiming that the changes introduced by the Council and the Parliament ‘seriously distort its proposal, interfere with some fundamental principles of the Treaty, with the institutional balance and with the independent exercise by the ECB of its monetary policy competence’ (ECB 2019). In particular, the central bank complained that its reliance on ESMA’s designation of third-country CCPs as ‘systemically important’ would deprive it of important discretionary powers over euro clearing. This would create ‘*de facto*, a hierarchy’ between measures adopted to protect the EU single market and the euro area, leaving the ECB’s competence subject to the decisions of a ‘Union agency’ (ECB 2019).

By contrast, ESMA welcomed the enhanced supervisory capabilities envisaged in EMIR II, but was keen to extend these powers further. The Chair of ESMA, Steven Maijoor, was critical of the Commission's original proposal – whereby ESMA would take the lead role, supported by the national competent authorities, the ECB and other central banks – as being 'too complex' and likely to generate 'turf wars' (Friedrich and Thiemann 2018). Instead, he argued that centralising CCP supervision within ESMA was essential to the effective enforcement of the single rulebook and the creation of a genuine single EU financial market (interview, Paris, July 2018; see Maijoor 2018). Furthermore, ESMA encouraged the Commission 'to consider whether similar proposals should be envisaged for other market infrastructures and key market players', such as 'credit rating agencies, trade repositories, benchmarks, and possibly trading venues, and data providers' (ESMA 2017). EMIR II was therefore widely interpreted as a power grab on the part of ESMA. One regulator noted that 'ESMA has pushed to the limits its existing powers...it is an open secret that ESMA wants to increase its powers, and this is its moment in the sun' (interview, London, August 2018), while another argued that ESMA had 'aspirations to become the equivalent of Securities and Exchange Commission in the US' (interview, London, June 2018).

The bureaucratic rivalry between ESMA and the ECB was also rooted in fundamental questions about the future of euro area integration. Brexit fuelled calls from prominent EU leaders for the EU and euro area to be more closely aligned (Brunsden and Stafford 2017), but this placed a question mark over the future of the European Supervisory Authorities (ESAs), like ESMA. While some advocated ESMA evolving to become a powerful securities regulator, others suggested that ESMA should be scrapped and responsibility for securities and market infrastructure centralised within the ECB, to mirror the arrangement for banking supervision. One interviewee stressed that this was now a 'key philosophical question' in

Brussels: ‘are we creating a regulatory superpower, the ECB, as an umbrella for ESAs and national competent authorities?’ (interview, Brussels, May 2018).

The response of third countries (and the UK) to EMIR II is best interpreted from a state-centric perspective. Unsurprisingly, the UK and the US firmly opposed the prospect of new restrictions on euro clearing in third countries, arguing that this would heighten financial stability risks and increase economic costs (Carney 2017). However, this masked important differences in both the preferences and strategies adopted by UK and US policy-makers. To the surprise of many, the Bank of England welcomed the EU’s proposal. Mark Carney, Bank of England Governor, recognised ‘the importance of effective cooperation arrangements between the relevant EU authorities and their overseas counterparts’ (cited in Vermuth 2017). Similarly, Andrew Bailey, head of the Financial Conduct Authority, argued that the legislation was ‘not a clear location policy saying you have to move...We know enough about how to do regulatory cooperation. We can make that work’ (cited in Maxwell 2017). The ‘constructive dialogue’ struck by UK regulators reflected the fact that they were relatively relaxed about the prospect of joint supervision of London-based CCPs with ESMA: this ‘best case scenario’ was viewed a price worth paying to ‘make sure that forced relocation [of euro clearing] never happens’ (interviews, London, May and August 2018). UK regulators, together with LCH, were also sanguine about the relocation of repo clearing to Paris in the hope that London could retain its dominance in clearing interest rate swaps (interview, London, September 2016).

Unlike UK policy-makers, the US authorities were more concerned about supervision than relocation. As a senior US regulator noted, ‘relocation is not really a concern for us. Our worst-case scenario is the EU gaining full joint supervision over US-based CCPs. The real

sensitivity for us is not what happens to US CCPs in London, but US CCPs at home’ (interview, London, July 2018). In particular, they objected to ESMA and the ECB gaining extraterritorial supervisory and oversight powers over all aspects of US CCPs, not just EU-related business, the prospect of which would almost certainly be ‘killed by Congress’. This position was articulated forcefully by senior US regulators. In an opinion piece provocatively titled ‘An EU plan to invade US markets’, Christopher Giancarlo (2017b), head of the CFTC, claimed that under the EU’s plans US CCPs would be subject to on-site inspections by ESMA and to additional rules by the ECB without consultation. He added that ‘such overlapping and uncoordinated regulation by the EU would be disruptive, expensive and detrimental to the US trading markets and economy’ (Giancarlo 2017b).

In a further ramping up of the rhetoric, Giancarlo argued that the EU’s ‘completely irresponsible’ legislation threatened to reopen the 2016 US-EU agreement on CCP regulation (Giancarlo 2017a), and that the US could retaliate by barring EU banks from using US exchanges. From the UK’s perspective, the US’s hostility to enhanced EU supervision of third-country CCPs was highly problematic. According to a senior UK regulator, ‘the EU assumes that the US simply sides with the UK on all these issues, which is not true. We are not completely aligned’ (interview, London, June 2018). As a result, the capacity of US and UK regulators to forge an ‘Anglo-American’ transgovernmental alliance against the EU’s plans was limited.

We find less evidence in support of a transnational governance perspective. In response to EMIR II, the cross-border derivatives industry initially attempted to form a transnational alliance in opposition to tougher clearing rules. For example, the four main international financial associations (GFMA, SIFMA, AFME, ASIFMA 2017) sought to present a united

front by submitting a joint response to the Commission's consultation.⁶ Scott O'Malia, chairman of ISDA, argued that new EU restrictions on third countries 'could have massive implications for efficient cross-border flows...which increases costs, risk and operational complexity for derivatives users' (Burton 2017). With the encouragement of UK officials, the London Stock Exchange – as the owner of one of the world's largest CCPs, LCH – was also particularly active in trying to build a transatlantic alliance. In particular, it sought to enlist the support of US policy-makers by establishing its first 'political action committee' to represent its interests in Washington. Yet, these efforts proved largely ineffective. EU regulators noted that LCH undermined its credibility by hastily publishing estimates of the economic costs of the EU's proposal, which later proved inaccurate. Moreover, the aggressive response of US regulators, and their heavy-handed attempt to lobby national supervisors and MEPs, was viewed by many as counterproductive: 'It has been a spectacular miscommunication and one of the best examples of how not to lobby in Europe, because they don't understand how it works or how to behave' (interview, Brussels, August 2018).

More importantly, industry-led efforts to forge a transnational alliance were constrained by divisions between the three main sets of actors involved (see Pagliari and Young 2014): end-users, CCPs, and dealer banks. The first group, financial/non-financial end-users, had a shared interest in resisting the imposition of new restrictions on euro clearing as this would raise costs for ordinary businesses that rely on derivatives to hedge risk. But end-users were ultimately too highly dispersed and weakly organised to mobilise collectively, or lobby effectively on this issue (interview, Brussels, May 2018). Second, the main CCPs were not a significant lobbying force because they constitute 'a small universe of players' and had widely divergent preferences on EMIR II. Existing global CCPs, predominantly based in London and New York, were highly critical of the EU's proposals, but for different reasons:

while LCH in London feared losing euro clearing business, CME in Chicago was primarily concerned about extraterritorial EU supervision (interview, London, July 2018). By contrast, rival EU CCPs, notably Deutsche Börse-owned Eurex Clearing in Germany, warmly welcomed the changes as they would centralise supervision and provide a competitive advantage over third-country CCPs. They also directly challenged the figures put forward by ISDA and LCH regarding the additional margin costs that relocation would impose (Jones 2017a). This fragmentation along national/regional lines prevented the main transnational trade associations – namely, ISDA, the European Association of Clearing Houses, and the European Banking Federation – from adopting policy positions that were unambiguously opposed to new euro clearing restrictions (interviews, London, Brussels, May-July 2018).

Surprisingly, we find that the most effective opposition to the potential relocation of euro clearing actually came from the third group: EU dealer banks based predominantly in France and Germany. They had two main concerns (interview, London, September 2018). First, the de-recognition of LCH by the EU could potentially impose huge additional capital costs on EU banks as they would be required to hold much greater collateral against pre-existing derivative contracts traded through London. This would hit the largest French and German banks, which are ‘massively exposed’ to clearing positions through LCH, particularly hard: Deutsche Bank, for example, made it known to the Bundesbank that the scale of these additional capital charges would be ‘existential’. Second, this problem could be avoided if dealer banks were able to unwind existing contracts from LCH and clear them through an EU CCP. But this process would be hideously complicated and time-consuming as every derivative trade between a buyer and a seller has to be ‘netted’ off against another to minimise risk exposure.

Contrary to what we would expect from a state-centric perspective, the main French and German banks found little sympathy from their home governments: ‘they got the message from their political connections that this was happening, so don’t annoy us’ (interview, London, September 2018). Instead, the banks began ‘quietly lobbying at the EU level...in a targeted way’ for EMIR II to be toned down. From an early stage these efforts were directed at the Commission, which was supplied with position papers detailing the costs of fragmenting euro clearing markets. This information was ‘helpful’ from the perspective of the Commission looking to push back against pressure from the ECB and French government (interview, London, September 2019), and was used to inform the Commission’s own Impact Assessment on the implications of relocation (Commission 2017b: 61-67). One lobbyist suggested that it was common for Commission officials to assist the banks in their efforts, helping to ‘steer our next steps’ by ‘telling us who we need to go and speak to’ in order to try to ‘unblock’ opposition from other EU institutions (interview, London, September 2019). Similarly, later in the legislative process, EU banks also worked closely with prominent MEPs on the ECON Committee who facilitated access by ‘feeding information...to inform the triologue negotiations’. By contrast, little attempt was made to lobby the ECB because it was viewed as less amenable to industry’s concerns. We suggest that this evidence fits well with a bureaucratic politics perspective because the influence of EU dealer banks relies less on transnational alliance-building, and more on the capacity to find sympathetic institutional sponsors at the EU level.

The final agreement on EMIR II, reached in March 2019, significantly strengthened EU-level supervision of CCPs both within and outside the EU. Importantly, however, the outcome was less ambitious than originally envisaged, in large part because it had to ‘thread the needle’ between competing bureaucratic positions (interview, London, July 2018). It established a

‘CCP supervisory committee’ within ESMA composed of a Chair and competent authorities of member states with an authorised CCP. Central banks of countries whose currency was used for the transaction would be allowed to participate on specific matters, without voting rights. The CCP supervisory committee would meet in two configurations: one for the supervision of CCPs based in the EU, the other for the supervision of third-country CCPs. Whereas the Committee was responsible for the recognition and supervision of third-country CCPs, the licensing and supervision of EU CCPs would remain the responsibility of national authorities, maintaining the existing fragmented supervisory structure. The modest changes in this respect reflected the influence of bureaucratic politics, albeit at the national level. National financial regulators, supported by several member state governments, were strongly opposed to the centralisation of supervisory competences over clearing houses at the EU level (Jones 2017).⁷ As one interviewee (London, June 2018) remarked, ‘member states focused their political capital more on the bits that concerned EU CCPs...as they did not want their national authorities to lose power’.

With respect to euro clearing, EMIR II was revised during the legislative process to make the prospect of relocation even less likely. In the Council, France, Germany and Italy were ardent supporters of tougher restrictions on third country clearing. Other EU member states were less enthusiastic as they had little at stake in the outcome, but were nonetheless willing to support the legislation (interviews, London, Brussels, May-July 2018).⁸ However, EMIR II faced greater opposition in the European Parliament. Like the Commission, MEPs were determined to uphold the interests of the EU institutions and the single market, and to avoid significantly raising clearing costs for banks and end-users (interview, Brussels, September 2018). The MEP rapporteur in charge of the dossier, Danuta Hübner, stated that relocation

should be ‘the last resort’ and argued that ‘the process of denying recognition should be made more fact-based and evidence-based’ (EP 2018).

To address these concerns, Parliament sought to ‘clip the wings’ of the legislation by making forced relocation more difficult (interview, Brussels, June 2018). This culminated in amendments, which required any decision to derecognise a third-country CCP to be subject to a rigorous economic impact assessment, and which granted a twelve-month ‘adaptation period’ for EU firms forced to relocate their euro clearing business. According to a senior EU legislator, the result was that relocation was reduced to ‘a threatening device, to get third country authorities to listen to the EU, on the assumption that in practice it will never be used’ (interview, Brussels, September 2018). In accordance with the Commission’s cautiousness over euro clearing, it was fully supportive of these changes, which were eventually included in the final legislation.⁹

6. CONCLUSION

The Brexit referendum in June 2016 reignited the sensitive issue of euro clearing, reviving memories of the ECB’s failed attempt to force relocation from London to the euro area at the height of the financial crisis. Despite this, the EU’s legislation fell significantly short of a location policy. Instead, EMIR II substantially strengthened the supervision of non-EU CCPs. The legislation left open the possibility of derecognising third-country CCPs where they were deemed ‘substantially systemically important’, which would force EU clients to relocate their clearing business to the EU27. However, a series of safeguards were put in place to ensure that there were very high barriers to doing so. To explain why the EU resisted concerted pressure from national governments and the ECB to introduce a strict location policy, we

adopted a synthesis approach combining theories with distinct domains of application to provide a more comprehensive explanation (Jupille et al 2003).

The article makes two main theoretical contributions to the literature on the political economy of finance in the EU and internationally. First, it assesses the explanatory power of well-established theories of political economy with reference to an important and understudied regulatory issue: euro-denominated clearing. In doing so, we find that while state-centric and transnational approaches have some explanatory leverage, they are also both characterised by important analytical blind spots. Specifically, state-centric perspectives explain why there was interest-based member state mobilization on this issue. But it leads to under-determined predictions about the outcome because it cannot explain why the EU resisted pressure to impose a location policy for euro clearing. In addition, transnational perspectives are not well placed to explain the weak organisation of cross-border financial interests, or the strongly nationally-embedded character of CCP allegiances.

Second, we argue that an important limitation of these perspectives is that they say relatively little about the critical role of supranational institutions in the EU. By reducing the preferences and actions of these institutions to either intergovernmental bargaining, or transnational interests, they are denied independent agency. To address this, we show that the incorporation of a bureaucratic politics perspective can add significant value to political economy explanations of EU financial regulation. For example, the capacity of the French and German governments to push for the relocation of euro clearing relied, in large part, on their alliance with the ECB; but that this was ultimately constrained by opposition from the Commission and Parliament. Conversely, although transnational financial interests played a largely back seat role, EU dealer banks were important because their interests were aligned

with the Commission and Parliament, enabling EU officials and MEPs to leverage their concerns against the ECB. The EU's cautiousness on euro clearing was therefore not simply the outcome of national competition or transnational lobbying. Rather, it was in large part rooted in divergent policy preferences and power dynamics between different supranational institutions, each of which was in competition to shape the regulatory agenda and expand their policy competences.

The analysis raises a number of important theoretical and empirical issues. The first is the need to clarify the contribution of a bureaucratic politics approach to the existing political economy literature. We argue that devoting greater attention to the EU inter-institutional dimension enables greater specificity with respect to political economy explanations. In particular, it serves to illuminate the 'scope' conditions for both state-centric and transnational explanations – that is, the explanatory limits of their 'domains of application' (Jupille et al 2003). For example, the study suggests that transnational explanations may be better suited to financial regulatory domains characterised by relatively few, large economic players with shared preferences (such as investment banking), which enables them to organise collectively, rather than domains characterised by multiple actors with divergent economic interests (such as derivatives). Furthermore, we find that state-centric explanations do a good job of explaining actor preferences (both government and industry) around regulatory issues with direct distributional implications, i.e. those that impose economic costs on different groups (such as the location of euro clearing). But they are less helpful at explaining regulatory outcomes concerned with the allocation of regulatory powers and policy competences (e.g. the supervision of EU and non-EU CCPs). In the case of euro clearing, the interconnectedness of these two dimensions makes the integration of a bureaucratic politics perspective essential.

The second issue concerns the ongoing uncertainty surrounding Brexit and the future UK-EU relationship. In the unlikely event that the UK remained in the single market (through EEA membership), London-based CCPs would undoubtedly be placed on a firmer regulatory and supervisory footing because of the direct application of EMIR II. However, as the UK would still become a third country, the Commission could still, in theory, require euro clearing at ‘substantially systemically important’ CCPs to be relocated to the EU27. Moreover, in practice calls to do so from France, Germany and the ECB would almost certainly continue. In the case of a no-deal Brexit, ESMA’s decision to grant permission to London-based CCPs to continue serving EU clients to minimise disruption only provides a transitory respite. Prolonged delay in reaching a comprehensive trade agreement covering financial services would certainly heighten political demands for relocation, and render London’s dominant position in the clearing of euro-denominated derivatives increasingly untenable.

ACKNOWLEDGEMENTS

We wish to thank the anonymous reviewers and the journal editors for their perceptive and constructive comments. We also benefited from presenting our paper at the 2019 Biannual Conference of the European Union Studies Association in Denver, the 2019 Annual Conference of the Council of European Studies in Madrid, and a research colloquium at the University of Bologna. We are particularly grateful to Simon Bulmer, David Howarth, Erik Jones, Aneta Spendzharova, Elliot Posner and Matthias Thiemann for their helpful advice and suggestions.

REFERENCES

Adolph, C. (2013) *Bankers, Bureaucrats and Central Bank Politics: The Myth of Neutrality* Cambridge: Cambridge University Press.

Autorité des Marchés Financiers (AMF) (2017) *Priorities in the EMIR Review*, May, Paris.

Bach, T., F. De Francesco, M. Maggetti and E. Ruffing (2016) 'Transnational bureaucratic politics: An institutional rivalry perspective on EU network governance', *Public Administration* 94 (1): 9–24.

Baldwin, R., Cave, M. and Lodge, M. (2013) *Understanding Regulation: Theory, Strategy and Practice* Oxford: Oxford University Press.

Bean, C. (2016) *Oral evidence*, Select Committee on the European Union, House of Lords, 7 September, London.

Brunsdon, J. and Stafford, P. (2017) 'London warns Brussels of risk in moving euro clearing business', *Financial Times*, 13 June.

Burton, L. (2017) 'US regulator warns Europe to tread carefully on euro clearing', *Telegraph*, 10 May.

Busuioc, M. (2016) 'Friend or foe? Inter-agency cooperation, organizational reputation and turf', *Public Administration* 94 (1): 40-56.

Büthe T, and Mattli W (2011) *The New Global Rulers: The Privatization of Regulation in the World Economy*, Princeton: Princeton University Press.

Canepa, F, Koranyi, B. (2017) 'Exclusive: ECB plan to take euro clearing from London stalled by infighting', *Reuters*, 22 May.

Carney, M. (2017) 'A Fine Balance', speech at Mansion House, 20 June, London.

Carpenter, D. P. (2001) *The Forging of Bureaucratic Autonomy: Reputations, Networks and Policy Innovation in Executive Agencies, 1862-1928*, Princeton: Princeton University Press.

Cerny, P. (2010) *Rethinking World Politics: A Theory of Transnational Pluralism*, Oxford: Oxford University Press.

Chicago Mercantile Exchange (CME) (2017) 'Response to Consultation re. EMIR review', 30 October, Chicago.

Clift, B. and Woll, C. (2012) 'Economic patriotism: reinventing control over open markets', *Journal of European Public Policy* 19 (3): 307-23.

Coen, D., & Thatcher, M. (2008) 'Network governance and multi-level delegation: European networks of regulatory agencies', *Journal of Public Policy* 28 (1):49–71.

Coere, B. (2017) 'Speech: European CCPs after Brexit', ECB, Frankfurt.

Commission (2017a) *Proposal concerning the procedures and authorities involved for the authorisation of CCPs and requirements for the recognition of third-country CCPs (EMIR II)*, 7 June, Brussels.

Commission (2017b) *Commission Staff Working Document: Impact Assessment (amending Regulation (EU) No 1095/2010 and Regulation (EU) No 648/2012* , 13 June, Strasbourg.

Djelic M-L, S. Quack (eds) (2010) *Transnational Communities: Shaping Global Economic Governance*, Cambridge: Cambridge University Press.

Dombret, A. (2017) 'Uncertain times - Brexit and its impact on the financial sector', 7 February, Bundesbank, Frankfurt.

Donnelly S. (2014) 'Power politics and the undersupply of financial stability in Europe', *Review of International Political Economy* 21 (4): 980-1005.

Drezner, D.W. (2007) *All Politics Is Global: Explaining International Regulatory Regimes*, Princeton: Princeton University Press.

Dunleavy, P. (1991) *Democracy, Bureaucracy and Public Choice*, Hemel Hempstead: Harvester Wheatsheaf.

Eberlein, B., and Newman, A. L. (2008) 'Escaping the international governance dilemma? Incorporated transgovernmental networks in the European Union', *Governance* 21(1): 25–52.

Egeberg, M., and Trondal, J. (2011) 'EU-level agencies: new executive centre formation or vehicles for national control?', *Journal of European Public Policy* 18 (6): 868-887.

European Central Bank (ECB) (2011) *Eurosystem Oversight Policy Framework*, 11 September, Frankfurt.

ECB (2015) *European Central Bank and Bank of England announce measures to enhance financial stability in relation to centrally cleared markets in the EU*, 29 March, Frankfurt.

ECB (2017) *Recommendation amending Article 22 of ECB Statute*, 23 June, Frankfurt.

ECB (2019) 'Letter concerning the Withdrawal of the Recommendation of the ECB for a Decision of the European Parliament and of the Council amending Article 22 of the Statute of the European System of Central Banks and of the European Central Bank', 20 March, Frankfurt.

Epstein, R. and M. Rhodes (2016) 'The political dynamics behind Europe's new Banking Union', *West European Politics* 39 (30): 415-37.

European Securities Markets Authority (ESMA) (2017) *Letter to European Commission on third-country regimes*, 10 July, Paris.

Farrell, H. and Newman, A. (2016) 'The new interdependence approach: theoretical development and empirical demonstration', *Review of International Political Economy* 23 (5): 713-736.

Farrell, H. and Newman A. (2014) 'The new politics of interdependence: Cross-national layering in Trans-Atlantic regulatory disputes', *Comparative Political Studies* 48 (4): 497–526.

Fioletos, O. (2010) 'Capitalist diversity and the international regulation of hedge funds', *Review of International Political Economy* 17 (3): 696–723.

Fioletos, O. (2011) *Creative Reconstructions: Multilateralism and European Varieties of Capitalism after 1950*, Ithaca: Cornell University Press.

Fouquet, H. and Detrixhe, J. (2016) 'Hollande takes aim at City of London in euro clearing threat', *Bloomberg*, 29 June.

Frankfurt Finance and Paris Europlace (2017) *Joint statement on euro clearing*, 12 July, Frankfurt.

Friedrich, J., and Thiemann, M. (2018) *A new governance architecture for European financial markets? Towards a European supervision of CCPs*, White Paper Series, No. 53, SAFE - Sustainable Architecture for Finance in Europe, Frankfurt, <http://nbn-resolving.de/urn:nbn:de:hebis:30:3-472301>

Gabor, D. (2016) 'The (impossible) repo trinity: the political economy of repo markets', *Review of International Political Economy* 23 (6): 967-1000.

Giancarlo, C. (2017a) *Future of CFTC-EU Regulatory Coordination in the Financial Sector*, 14 September, Washington.

Giancarlo, C. (2017b) *An EU plan to invade the US market*, 6 November, Washington.

Goldbach, R. (2015a) *Global Governance and Regulatory Failures*, Basingstoke: Palgrave

Goldbach, R. (2015b) 'Asymmetric influence in global banking regulation, transnational harmonization, the competition state, and the roots of regulatory failure', *Review of International Political Economy* 22 (6): 1087–1127.

Gravelle, M. and Pagliari, S. (2018) 'Global markets, national toolkits', in Helleiner, E., Pagliari, S. and Spagna, I. (eds) *Governing the World's Biggest Market: The Politics of Derivatives Regulation After the 2008 Crisis*, Oxford: Oxford University Press.

Grant, C. (2009) 'Banque de France in CDS clearing plea', *Financial Times*, 17 February.

Graz, C., Noelke, A. (eds) (2008) *Transnational Private Governance and its Limits*, London: Routledge.

GFMA, SIFMA, AFME, ASIFMA (2017) *Response to consultation EMIR review*, 30 October, Brussels.

Helleiner, E. (2014) *The Status Quo Crisis: Global Financial Governance After the 2008 Financial Meltdown*, Oxford: Oxford University Press

Helleiner, E., Pagliari, S and Spagna, I. (eds) (2018) *Governing the World's Biggest Market: The Politics of Derivatives Regulation After the 2008 Crisis*, Oxford: Oxford University Press.

Howarth, D., and Quaglia, L., (2018) 'Brexit and the battle for financial services', *Journal of European Public Policy* 25 (8): 1118-1136.

Howarth, D., Quaglia, L., (2017) 'Brexit and the Single European Financial Market', *Journal of Common Market Studies Annual Review* 55 (s1): 149–164.

Howarth D. and Quaglia L. (2016) 'The comparative political Economy of Basel III in Europe', *Policy and Society* 35 (3): 205-214.

Hope, K. (2017) 'What on earth is euro clearing - and why should you care?', *BBC News*, 13 June.

Intercontinental Exchange (ICE) (2016) *Access to global markets to sustain jobs and growth: A financial infrastructure perspective*, Working paper, https://www.theice.com/publicdocs/ICE_Working_Paper_Access_Global_Markets.pdf

International Swaps and Derivatives Association (ISDA) (2017) *Response to consultation EMIR review*, 30 October, London.

Jabko, N. (2006) *Playing the Market: A Political Strategy for Uniting Europe, 1985-2005*, Ithaca: Cornell University press.

Jones, H. (2017a) 'Derivatives body warns EU against moving euro clearing from London', *Reuters*, 12 June.

Jones, H. (2017b) 'France wants right to Veto Euro Clearing in the UK after Brexit ', *Reuters*, 6 September

Jupille, J., Caporaso, J. A. and Checkel, J. T. (2003) 'Integrating Institutions: Rationalism, Constructivism and the Study of the European Union', *Comparative Political Studies* 36 (1/2): 7-40.

Knaack, P. (2015) 'Innovation and deadlock in global financial governance: transatlantic coordination failure in OTC derivatives regulation', *Review of International Political Economy* 22 (6):1-32.

Krause, G. A. and Meier, K. J. (eds.) (2003), *Politics, Policy and Organizations: Frontiers in the Scientific Study of Bureaucracy*, Ann Arbor: University of Michigan Press.

Lannoo, K. (2017) *Derivatives Clearing and Brexit*, Bruegel N 25, November, Brussels.

Lavery, S., Quaglia, L. and Dannreuther, C. (2018), 'Brexit and the Future of British Capitalism: First Symposium', *New Political Economy*, <https://www.tandfonline.com/doi/full/10.1080/13563467.2018.1484716>

London Stock Exchange (LSE) (2017) *Response to EMIR consultation*, 30 October, London.

Maxwell, F. (2017) 'City cheers looming end of euro-clearing oversight, *Politico*, 7 July.

McKeen-Edwards, H. and Porter, T. (2013) *Transnational Financial Associations and the Governance of Global Finance*, London: Routledge.

Macartney, H. (2010) *Variiegated Neoliberalism: EU varieties of capitalism and International Political Economy*, London: Routledge.

Maor, M. (2010) 'Organizational reputation and jurisdictional claims: The case of the U.S. food and drug administration', *Governance* 23(1): 133-159.

Mersch, E. (2017) *Evolving regulatory environment for CCPs – the perspective of a Central Bank*, ECB, Frankfurt, available at <http://www.ecb.europa.eu/press/key/date/2017/html/ecb.sp171110.en.html>

Mügge, D. (2010) *Widen the Market, Narrow the Competition: Banker Interests and the Making of a European Capital Market*, Colchester: ECPR.

Newman, A. Bach, D. (2014) 'The European Union as hardening agent: soft law and the diffusion of global financial regulation', *Journal of European Public Policy* 21 (3): 430-452.

Newman, A., and Posner, E. (2018) *Voluntary Disruptions. International Soft Law, Finance, and Power*, Oxford: Oxford University Press.

Newman, A. and Posner E. (2016) ‘Transnational feedback, soft law, and preferences in global financial regulation’, *Review of International Political Economy* 23 (1): 123-152.

Oliver Wyman (2016) Report on ‘The Impact of the UK’s Exit from the EU on the UK-Based Financial Services Sector’, available at https://www.oliverwyman.com/content/dam/oliverwyman/global/en/2016/oct/Brexit_POV.PDF

Pagliari, S. (2013) ‘A wall around Europe? The European regulatory response to the global financial crisis and the turn in Transatlantic relations’, *Journal of European Integration* 35(4): 391–408.

Pagliari S., Young K.L (2014) ‘Leveraged interests: Financial industry power and the role of private sector coalitions’, *Review of International Political Economy* 21 (3): 575–610.

Peters, G.B. (2002) *The Politics of Bureaucracy*, London: Routledge.

Porter, T. (2014) ‘Technical systems and the architecture of transnational business governance interactions’, *Regulation and Governance* 8: 110–125.

Posner, E. (2010) ‘The Lamfalussy Process: Polyarchic Origins of Networked Financial Rulemaking in the EU,” in *EU Governance: Towards a New Architecture?* (eds.), Charles F. Sabel and Jonathan Zeitlin, Oxford: Oxford University Press, pp.43-60.

Posner, E. (2009) *The Origins of Europe's New Stock Markets*, Harvard: Harvard University Press.

Rixen, T. (2013) 'Why reregulation after the crisis is feeble: Shadow banking, offshore financial centers, and jurisdictional competition', *Regulation & Governance* 7 (4): 435–459.

Rixen, T. (2010) 'Bilateralism or multilateralism? The political economy of avoiding international double taxation', *European Journal of International Relation* 16 (4): 589–614.

Rolet, X. (2016) 'Oral Evidence, Brexit: financial services', 9th Report of Session 2016-17, European Union Committee, House of Lords, December.

Rosamond, B. (2012) 'Supranational governance as economic patriotism? The European Union, legitimacy and the reconstruction of state space', *Journal of European Public Policy* 19 (3): 324-341.

Seabrooke, L. and Henriksen, L.F. (eds) (2017) *Professional Networks in Transnational Governance*, Cambridge: Cambridge University Press

Seabrooke, L. and Wigan, D. (2016) 'Powering ideas through expertise: professionals in global tax battles', *Journal of European Public Policy* 23 (3): 357–74.

Stone, D., and Ladi, S. (2015) 'Special Issue: Symposium: Global Policy and Transnational Administration', *Public Administration*, 93 (4).

Stafford, P. (2017) 'Deutsche Börse eyes City of London's euro clearing crown', *Financial Times*, 20 November.

Storbeck, O. (2018) 'Deutsche Bank shifts half of euro clearing from London to Frankfurt', *Financial Times*, 29 July.

Thiemann, M. (2018) *The Growth of Shadow Banking: A Comparative Institutional Analysis*, Cambridge: Cambridge University Press.

Thiemann, M. (2014) 'In the shadow of Basel: How competitive politics bred the crisis', *Review of International Political Economy* 21 (6): 1203–1239.

Trondal, J., Marcussen, M., Larsson, T., Veggeland, F. (2013) *Unpacking International Organisations: The Dynamics of Compound Bureaucracies*, Manchester: Manchester University Press.

Tsingou, E. (2015) 'Club governance and the making of global financial rules', *Review of International Political Economy* 22 (2): 225–256.

Tucker, P. (2011) 'Speech given the the Financial Innovation (CSFI) Post Trade Fellowship Launch', 11 June, London.

Verdun, A. (2017) 'Political leadership of the European Central Bank', *Journal of European Integration* 39 (2): 207-221.

Wagstyl, S. and Chazan, G (2016) ‘Wolfgang Schäuble sets out a tough line on Brexit’, *Financial Times*, 17 November.

Wermuth, T. (2017) ‘Carney warns EU against splitting euro clearing market’, *Reuters*, 20 June,

Wilson, J.Q. (1989) *Bureaucracy: What Government Agencies Do and Why They Do It*, Basic Books.

Young, K. (2012) ‘Transnational regulatory capture? An empirical examination of the transnational lobbying of the Basel Committee on Banking Supervision’, *Review of International Political Economy* 19 (4): 663–88.

¹ Henceforth we refer to the 2011 ECB proposal as a ‘location policy’, and to the requirements for euro clearing envisaged in the proposal for EMIR II as ‘euro clearing restrictions’.

² The dealer banks are: Bank of America, Barclays, BNP Paribas, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JPMorgan Chase, Morgan Stanley, Royal Bank of Scotland, Société Générale, UBS, Wells Fargo, Credit Agricole and Nomura.

³ The document is not publicly available. Its existence and content were reported by Financial News, 19 February 2009 ‘French working group readies a clearing assault’, available at <https://www.fnlondon.com/articles/french-working-group-readies-a-clearing-assault-1-20090219>

⁴ Equivalence rules stipulate that unless third country rules are equivalent to EU rules, foreign firms providing services in the EU or doing business with EU counterparts would be subject to EU regulation in addition to their home country regulation. Without equivalence, foreign firms failing to respect EU regulations would be blocked from accessing the Single Market.

⁵ See https://ec.europa.eu/info/sites/info/files/economy-finance/c2017-6810_annex_en.pdf

⁶ The consultation responses to the Commission’s proposal reveal that most industry responses came from third country entities and transnational business associations. Of the 18 responses, six came from the US, four from the UK, four from Brussels, two from Germany, one from France, and one from Austria.

⁷ German supervisors, in particular, were very reluctant to relinquish responsibility for supervising Eurex Clearing in Frankfurt, arguing that the EU should ‘not try to fix what is not broken’, and insisting that the ECB and ESMA should only be given an advisory role (interview, Brussels, July 2018).

⁸ Sweden and Poland echoed the Commission’s concern that new euro clearing restrictions should not be used to disadvantage non euro area states.

⁹ In a further softening of the EU’s position, the Commission issued a temporary equivalence decision, whereby the regulatory framework applicable to CCPs in the UK would be considered as equivalent to the one in the EU, in the event of a no deal Brexit. Subsequently, ESMA also recognised UK-based CCPs in order to ensure continued access of EU-based companies to their clearing services. See <https://www.esma.europa.eu/press-news/esma-news/esma-ready-review-uk-ccps%E2%80%99-and-csds%E2%80%99-recognition-applications-no-deal-brexit>