



European Securities and
Markets Authority

Consultation Paper

ESMA's Guidelines on CCP conflicts of interest management



Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

1. respond to the question stated;
2. indicate the specific question to which the comment relates;
3. contain a clear rationale; and
4. describe any alternatives ESMA should consider.

ESMA will consider all comments received by 24 August 2017.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

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

Data protection

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

Who should read this paper?

This consultation paper may be specifically of interest to CCPs, clearing members and more broadly to all stakeholders involved in clearing flows as well as of interest to trade associations.

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1 Executive Summary

Reasons for publication

EMIR only prescribes generic provisions in relation to the management by CCPs of conflicts of interest. Building on ESMA's experience in CCP colleges, it appears further guidance on CCPs management of conflicts of interest would be beneficial and further facilitate supervisory convergence on this area. The purpose of these Guidelines is thus (i) to set out the criteria CCPs should apply to avoid or mitigate the risks of conflicts of interest and (ii) to ensure a consistent implementation across CCPs.

Contents

The present report contains a proposal of guidelines on CCP conflicts of interest management. It is divided in four sections. Section 1 refers to the Executive Summary of the report. Section 2 establishes the legal background of the Guidelines, which come under EMIR and the ESMA's mandate, while Section 3 outlines the scope and the content of the proposed guidelines. Section 4 presents the proposed provisions of the guidelines on the CCP conflicts of interest management and a list of questions on the different topics. The Annex includes the summary of questions posed by ESMA and a preliminary cost-benefit analysis.

Next Steps

ESMA will consider the feedback it receives to this consultation in the second half of 2017 and expects to publish a final report of these Guidelines by the end of 2017.

2 Background and mandate

1. Under EMIR, central counterparties (CCP) shall act in the best interests of its clearing members and the clients. In that sense, CCPs shall have robust organisational arrangements and policies to prevent potential conflicts of interest and to solve them if the protective features are not sufficient.
2. To that end, Article 26 et seq. of EMIR and Article 3 et seq. of Commission Delegated Regulation (EU) 153/2013 of 19 December 2012 on requirements for CCPs define organisational rules aiming to achieve the above objectives.
3. More specifically, Article 33 of EMIR states the requirements in terms of management of conflicts of interest by CCPs. In particular, CCPs shall have written organisational and administrative arrangements to (i) identify and manage any potential conflicts of interest between itself and its clearing members or their clients known to the CCP, (ii) where the organisational or administrative arrangements of CCPs to manage conflicts of interest are not sufficient to ensure that risks of damage to the interests of a clearing member or client are prevented, it shall clearly disclose the general nature or sources of conflicts of interest to the clearing member or to the client before accepting new transactions from that clearing member, and (iii) where the CCP is a parent undertaking or a subsidiary, any circumstances of which the CCP is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other undertakings with which it has a parent undertaking or a subsidiary relationship shall be taken into account. The written arrangements shall include (i) the circumstances, which constitute or may give rise to a conflict of interest entailing a material risk of damage to the interests of one or more clearing members or clients, and (ii) the procedures to be followed and the measures to be adopted in order to manage such conflict.
4. As part of its CCP college activity, and given that ESMA is a member of all CCP colleges, ESMA has an horizontal view on how all EU CCPs have implemented these requirements. Over time, ESMA has identified a number of best practices as well as a range of more divergent approaches to the management of conflicts of interests.
5. In view of these observations and given that supervisory convergence in relation to CCPs is one of ESMA's key priorities, this document has been developed building on the best practices identified across the EU CCP policies and procedures with the objective to provide further guidance and ensure a consistent implementation of the EMIR requirements.
6. Under Article 16 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (ESMA), ESMA shall issue guidelines and recommendations to ensure a common, uniform and consistent application of the Union law.

3 Analysis

3.1 Scope of the guidelines

7. As EMIR only prescribes general requirements, these guidelines further specify Article 33 of EMIR regarding the management of the conflicts of interest by the CCPs.

3.2 Content of the guidelines

8. These guidelines firstly define what constitute a conflict of interest and what should be scope of the CCP policy regarding the conflicts of interest. Secondly, the guidelines describe the organisational arrangements the CCP should take in order to avoid or mitigate the conflicts of interests including the specific situation where the CCP is part of a group. Finally, the guidelines envisage the procedure the CCP should implement to solve the conflicts of interest.

4 Proposed guidelines

4.1 Scope

Who?

9. The adopted guidelines will apply (i) to competent authorities supervising central counterparties (CCPs) under Article 16 of Regulation (EU) No 648/2012 (EMIR) and (ii) to CCP authorised under Article 14 of EMIR.

What?

10. The adopted guidelines will apply in relation to CCP management of conflicts of interest.

When?

11. These guidelines apply from [date].

4.2 Definitions

12. Unless otherwise specified, terms used in the EMIR have the same meaning in these guidelines. In addition, the following definitions apply:

<i>EMIR</i>	European Market Infrastructures Regulation – Regulation (EU) 648/2012 of the European Parliament and Council on OTC derivatives, central counterparties and trade
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<i>EU</i>	European Union
<i>ESMA</i>	European Securities and Markets Authority
<i>OTC</i>	Over-the-counter
<i>Relevant person</i>	staff and their close family relationship as spouses, civil partner, other life companion, dependant persons as children and step-children, other relatives who permanently sharing the same household and relatives by blood or marriage up to the second degree, and any external person involved in the CCP business: risk committee members, remuneration committee members, default management group members, any other committee members, consultants, external advisors, agency, contract staff and subcontractors.
<i>Staff</i>	The CCP board members, directors, senior managers, managers and employees.

4.3 Purpose

13. The purpose of these guidelines is to ensure common, uniform and consistent application of the Articles 33 of EMIR and Article 3 et seq. of the Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 on requirements for CCPs.

4.4 Compliance and reporting obligations

4.4.1 Status of the guidelines

14. This document contains guidelines issued under Article 16 of the ESMA Regulation. In accordance with Article 16(3) of the ESMA Regulation competent authorities and financial market participants must make every effort to comply with guidelines and recommendations.
15. Competent authorities to whom the guidelines apply should comply by incorporating them into their supervisory practices, including where particular guidelines within the document are directed primarily at financial market participants i.e. CCP authorised under Article 14 of EMIR.

4.4.2 Reporting requirements

16. Competent authorities to which these guidelines apply must notify ESMA whether they comply or intend to comply with the guidelines, with reasons for non-compliance, within two months of the date of publication by ESMA to EU-CCP@esma.europa.eu. In the

absence of a response by this deadline, competent authorities will be considered as non-compliant. A template for notifications is available at the ESMA website.

17. Financial market participants to which these guidelines apply shall report to their competent authorities, in a clear and detailed way whether they comply with these guidelines.

4.5 Guidelines on CCP Management conflicts of interest

4.5.1 Definition and scope of conflicts of interest

18. A conflict of interest exists when a stakeholder's own interests interfere with the CCP's interests or the CCP's clients' interests in its objectivity to make decision or in its decision-making processes which it has to make in the course of its professional obligations.

19. The following source of the potential conflicts of interests should at least be considered by the CCPs:

- between the CCP and other group entities,
- between the CCP and any shareholder which at least own a holding over the thresholds set out in Article 31 of EMIR;
- between the CCP and the companies in which board member or a committee member performs other functions;
- between the CCP and a relevant person;
- between the CCP and a clearing member;
- between the CCP and a clearing member' client, if known to the CCP;
- between the CCP and a trading venue, a securities settlement system, a central securities depository, a trade repository, a data provider, a liquidity provider, a custodian bank, a settlement bank, a payment system, a payment agent, a nostro agent or any other service providers to the CCP;
- between the CCP and an interoperable CCP;
- between clearing members, clients or between a clearing member and a client.

20. CCPs should define a length of time during which the potential or real conflicts of interest are presumed to continue to have effects after the conflict ceased. Different timelines may be set-up by the CCPs depending on the type of conflict situation or concerned relevant person.

Q1. Do you agree with the definition and with the scope here above described?

4.5.2 Organisational arrangements

4.5.2.1 Need-to-know basis

21. CCPs should clearly implement organisational arrangements aiming at precluding the undue exchange or inappropriate use of confidential information within the CCP. CCPs should ensure that confidential information which, if known, would result in conflicts of interest is shared on a “need to know” basis. CCPs should put in place the necessary Chinese walls in the setting-up of its organigram to guarantee a clear separation of the work streams. The access to the IT system should be protected by the use of the appropriate security measures.
22. The informed staff members should be reminded that information must be kept internally and externally confidential and to not use such information to their own advantage. In case confidential information is shared with subcontractors or consultants, they should also be reminded that information must be kept internally and externally confidential and to not use such information to their own advantage.
23. In this framework, staff members and clearing members involved in the risk committee and in the default management groups should be subject to strict confidentiality obligations and should sign a specific confidentiality agreement. This should also apply to subcontractors or consultants if in their functions they access confidential information.

Q2. Do you think that the CCPs should implement such organisational arrangements to avoid an inappropriate use of confidential information?

4.5.2.2 Rules of conduct

24. CCPs should take the necessary measures for their staff members to :
 - act with impartiality and good faith, in the CCP interests, in a transparent manner and in compliance with the regulations
 - avoid a situation in which they have or can have a direct or indirect interest that conflicts with the CCP's interests.
25. CCPs should make ensure that they can take disciplinary actions against staff members breaching the above requirements.

26. CCPs should:

- adopt rules related to the limitation of the number of contracts or mandates board members and executive directors may have;
- not appoint an external auditors having a link with or receiving benefit from the CCP;
- require that the staff member disclose its personal interests and its close family relationship's interests which conflict or may conflict with the CCP's interests where the person is hired or nominated, updated where the situation changes and at least annually and when the conflicts of interest is no longer applicable;
- require that an employee which intends to perform any outside activity potentially conflicting with the responsibilities undertaken at the CCP seeks the CCP pre-approval before accepting the new engagement for another entity.

Q3. Do you consider that the proposed rules of conduct as appropriate to limit the risks of conflicts of interest?

4.5.2.3 Remuneration and gifts

27. CCPs policy should contain clear rules regarding the acceptance of the gifts whatever their form such as presents, inducements, preferential treatments, entertainment or hospitality received by any staff member from clearing members, clients, trading venue, central securities depositories, trade repositories, data providers, liquidity providers or any other service providers, subcontractors or any other person or entity which may have conflicting interests with the CCP.

28. In that sense, CCPs should set up a threshold in a reasonable manner to determine if the beneficiary is allowed to accept or to keep the gift. In case of doubt on the value of the gift, the chief compliance officer in principle is in charge to decide.

Q4. Do you believe that the CCPs should apply such rules concerning the gifts?

4.5.2.4 Ownership of financial instruments

29. CCPs should adopt policies defining rules on the ownership of financial instruments such as shares, bonds or any other securities that grant the right to acquire such securities which may create conflicts of interest.

30. CCPs should adopt strict rules to limit or monitor the staff investments: pre-approval and/or restrictions to invest and disinvest in financial instruments which might raise conflicts of

interest such as those issued by competitors, clearing members, clients, financial institutions and services providers should be requested by the CCPs. Exclusion or restriction periods to engage in transactions involving the securities of entities in the CCP group, such as during the month of the publication of the financial results or on an ad hoc basis may be considered by the CCPs. The rules may be adapted depending on the type of staff members concerned in order to ensure their accuracy and their effectiveness.

31. Direct investment carried out by any staff member should be disclosed to the chief compliance officer. The disclosure of the portfolio should be done at least at the hiring or nomination of any staff member and be updated annually. Any transactions on the concerned financial instruments executed should be reported to the chief compliance officer.
32. Where the investments are fully delegated to an investment company or are in UCITS or AIFM, the CCP should consider whether these investments should be excluded from the pre-approval and any restrictions, and from the disclosure obligation.

Q5. Are you in favour that CCPs should adopt the above clear rules on the ownership of the financial instruments?

4.5.2.5 Training

33. CCPs should make sure that its staff are adequately trained on their obligations and on the applicable procedure concerning the conflicts of interest management.
34. The training should clarify what constitutes a conflict of interest, the applicable regulation and penalties, the obligations of the staff, the declaration procedure and the resolution procedure of the conflict. The CCP should keep them updated on a regular basis.
35. The trainees should acknowledge that they are aware of the applicable rules. The CCP should keep a record of the training undertaken and completed by the staff.

Q6. Do you consider that the CPP staff should be trained on the applicable law and policies concerning the conflicts of interest as above described?

4.5.2.6 Oversight

36. In its responsibilities to oversight the compliance function, the CCPs' board should monitor the efficiency of the CCP arrangement to prevent and manage the conflicts of interest. The chief compliance officer should report to the board the material cases as defined by the CCP in a timely manner and its activities performed during the year.

37. The conflicts of interest policy should be at least reviewed by the compliance officer and the board where relevant, on a yearly basis, or earlier if significant amendments are required.
38. The audit department should assess the effectiveness of the conflicts of interest policy and of the overall CCP organisation linked to it on a regular basis.

Q7. Do you agree on the above-proposed rules?

4.5.3 Additional measures for CCPs belonging a group

4.5.3.1 At the level of the group

39. CCPs should be well-represented and in a balanced manner at the level of board of the mother company and, where relevant, of other subsidiaries linked to the CCP as trading feed, service provider, interoperable CCP, etc., in particular where sister CCPs are also represented.
40. The role of each board entities which are conflicted or potentially conflicted (such as the board of the mother company, the CCP's board, the board of the service provider) should be clearly defined and delineated to prevent overlapping competencies. Reserved matters dedicated to the CCP notably on the risk management matters should be prescribed.
41. Where necessary, at the level of the group, a procedure to resolve in a fairly, independent and efficient manner the conflicts of interest between the CCP and other group entities should be adopted.

4.5.3.2 At the level of the CCP board or supervisory board

42. To guarantee the CCP independence in accordance with Article 3 of the Commission Delegated Regulation (EU) No 153/2013, where needed, supplementary independent board members compared to the regulatory requirements should be appointed by the CCP to counterbalance the number of representatives of the group entities.
43. To be qualified as independent, the board member, its family or other relevant relationship should not have business that raises a conflict of interest regarding the CCP or its controlling shareholders, its management or its clearing members.

4.5.3.3 At the level of the CCP senior management or the management board

44. Where the senior management (i.e. the executive directors) is shared with another group entity, the CCP should compose its board or supervisory board of members in a way to ensure that an independent body monitors the CCP management's activities.

45. The material decisions should be approved by the board. To do so, a list of matters and/or criteria to identify the materiality of the decision to be taken directly by the board should be defined.

46. The senior management's responsibilities should be clearly defined, the wage including the bonuses of the senior managers should be correctly balanced compared to the one attributed by the other company in order to avoid any biased decision. A close monitoring of the potential conflicts of interest should be performed by the chief compliance officer, the board or the independent board members.

4.5.3.4 At the level of the staff

47. Where the CCP staff perform task for several group entities, the following rules should be adopted by the CCPs:

- the responsibilities, the distribution of working time and the hierarchical lines between the entities should be clearly defined. The CCP should check that the worktime for performing the several functions within different group entities is not higher than a full time job;
- the CCP should be fully part of the recruitment process and should have an effective power of decision on the selection of the employees, on their career progression or on the termination of the relationships. The CCP should continuously monitor the level of its human resources and have clear organigrams identifying shared resources.

48. The wage including bonuses of the concerned staff should be correctly balanced compared to the one attributed by the other company in order to avoid any partial decision or performance of tasks. The level of the bonuses or any other financial advantage rewarding the employees' performance in the CCP tasks should be assessed and ultimately decided by the CCP.

4.5.3.5 In case of outsourcing to another group entity

49. Where the service provider is part of the CCP's group, at least, the following supplementary measures should be taken by the CCP:

- the outsourcing of major activities to a group entity should be decided by the CCP board after, if relevant, seeking advice from the risk committee;
- the board should define the requirements of the services outsourced to other group entities;
- the CCP should check if the subcontractor has appropriate control arrangements in place to avoid conflicts of interest from their side in particular where the subcontractors provide a range of services to the CCP;

- the outsourcing arrangement should be performed under normal market conditions and should include provisions in respect of escalation and exit management;
- key performance indicators should be clearly defined and penalties in line with the standard market practices should be fixed and enforced if necessary. The subcontractor performance should be reported to the board;
- where the IT is outsourced, clear rules of prioritisation of the IT projects and change requests should be defined. Any change requests or project necessary to the CCP to comply with the regulation or any request from the competent authority should be implemented by the subcontractor in timely manner.

Q8. Do you agree on the above specific organisational arrangements a CCP pertaining to a group should adopt to avoid and mitigate the risk of conflicts of interest?

4.5.4 Conflicts of interest management procedure

4.5.4.1 Resolution procedure

50. Where an identified or possible conflict of interest appears during the course of the business relationship, it should be immediately and directly disclosed to the chief compliance officer and any other relevant person or body by the conflicted staff member or any other staff member aware of it as soon as reasonable possible.
51. The CCP should not require evidence of the conflicts of interest to be disclosed.
52. In case it is not certain whether a situation constitutes a potential or a current conflict of interests, the chief compliance officer should be in charge to clarify it.
53. The whistle-blower should not be blamed in any circumstance if it raises a conflict or potential conflict of interests.
54. The resolution procedure of the CCP should clearly identify the person in charge of the investigations if necessary, and the persons responsible for the decision-making. The decisions should be made by a person or a body which has sufficient independence and authority to enforce its decision. Several persons or bodies may be defined for that purpose depending on their responsibilities. The conflicted person should be heard during the process.
55. An escalation procedure should be implemented by the CCP in case of disagreement on the taken decision. The procedure should ensure that the case is heard in a short notice. At the latest stage, the independent board members might make the final decision.

4.5.4.2 Resolution measures

56. At least, the following range of measures to remedy probable or existing conflicts of interest should be envisaged by the CCPs:

- the monitoring of the conflict by the relevant body or staff member such as the board or the line manager;
- the disclosure to the affected party such as clearing member(s) or client(s) in a timely manner in compliance with Article 33(2) of EMIR;
- the exclusion of the conflicted staff member from the sensitive information;
- restriction to participate in the discussions, negotiations, decisions or votes which may be subject to a conflict of interest;
- exemption of duties and assignment to another staff member;
- temporary or definitive exclusion of the conflicted staff member to the relevant board, committee, meeting, etc.;
- the termination of the contract of the conflicted staff member;
- the disclosure to the national competent authorities.

4.5.4.3 Following-up

57. The chief compliance officer should verify on a regular basis the status of the conflict (i.e. potential/existing conflict of interest) and that the mitigation measures are enforced. The chief compliance officer should review if the measures are still necessary or need to be adapted. The frequency of the review should be adapted to the specificities of the cases.

58. The chief compliance officer should report to the board the conflicts of interest that have been occurred and any mitigating measures which have been decided on an annual basis.

59. In case of breach of the policy, the CCP should report any material breach to the national competent authority within 48 hours.

4.5.4.4 Conflicts of interest register

60. CCP should implement a register to track and record:

- the interests which potentially or concretely conflict with the CCP's interests disclosed by the staff members;
- the investments in financial instruments owned by the staff and any transactions related to it;

- the gifts above the threshold received by the staff and the decision related to it;
- the different steps of the resolution procedure;
- the resolution measures taken by the CCP;
- the reviews of the status of the conflicts of interest and the monitoring of the implementation of the resolution measures;
- the training performed by the staff.

61. The CCP should protect the personal data in accordance with the applicable EU Directive¹.

Q9. Do you think that the above-described procedure is appropriate to investigate, to solve, to monitor and to record the conflicts of interest?

¹ Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data.
Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation).

5 Annexes

5.1 Annex I – Summary of questions

Q1. Do you agree with the definition and with the scope here above described?

Q2. Do you think that the CCPs should implement such organisational arrangements to avoid an inappropriate use of confidential information?

Q3. Do you consider that the proposed rules of conduct as appropriate to limit the risks of conflicts of interest?

Q4. Do you believe that the CCPs should apply such rules concerning the gifts?

Q5. Are you in favour that CCPs should adopt the above clear rules on the ownership of the financial instruments?

Q6. Do you consider that the CPP staff should be trained on the applicable law and policies concerning the conflicts of interest as above described?

Q7. Do you agree on the above-proposed rules?

Q8. Do you agree on the above specific organisational arrangements a CCP pertaining to a group should adopt to avoid and mitigate the risk of conflicts of interest?

Q9. Do you think that the above-described procedure is appropriate to investigate, to solve, to monitor and to record the conflicts of interest?

5.2 Annex II – Preliminary high level cost-benefit analysis

1. Article 16 of the ESMA Regulation requires ESMA, where appropriate, to analyse the potential costs and benefits relating to proposed guidelines. It also states that cost-benefit analyses must be proportionate in relation to the scope, nature and impact of the proposed guidelines.
2. The objective of performing a cost-benefit analysis is to assess the costs and benefits of the various policy or technical options which were analysed during the process of drafting the guidelines.
3. The guidelines included in this CP are of an optional nature, i.e. they are not envisaged in any Regulation, but are issued in line with Article 16 of ESMA Regulation in order to ensure uniform, consistent and coherent application of Union Law.
4. The choices or options envisaged by ESMA while drafting these guidelines were therefore limited to whether to issue these guidelines and ensure a consistent application of EMIR within the Union (which is one of ESMA's tasks) or not issuing them.
5. There are directly applicable provisions in EMIR that would not apply in a uniform, consistent and coherent way within the Union in the absence of a clarification from ESMA on CCP conflicts of interest management.
6. The costs implied by these guidelines can be summarised as the cost of changing current CCP practices, where necessary.
7. These guidelines aim at ensuring the uniform, consistent and coherent application of EMIR across the Union, which is an essential component of an EU Regulation that by its nature is directly applicable in all Member States. In particular, these guidelines should help bringing more homogeneity in the content and presentation of rules and procedures established by the various CCPs, thus giving more clarity to the CCPs as to the way they should handle with the conflicts of interest.
8. Based on the analysis above, ESMA concludes that the benefits of issuing guidelines outweigh the costs.