Eurex Clearing Response to the

Consultation Paper on ESMA's Guidelines on CCP conflict of interest management

Frankfurt am Main, 24 August 2017

A. Introduction

Eurex Clearing is part of the Deutsche Börse Group providing central clearing services for cash and derivatives markets both for listed as well as certain over-the-counter (OTC) financial instruments.

Eurex Clearing is an EMIR authorized CCP incorporated in Germany and is also licensed as a credit institution under supervision of the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) pursuant to the Banking Act (Kreditwesengesetz).

Eurex Clearing appreciates the efforts of ESMA to align practices in Europe in conflicts of interest management and welcomes the opportunity to comment on the Consultation Paper on ESMA's Guidelines on CCP conflicts of interest management.

B. General comments

Eurex Clearing's conflicts of interest management is based on the requirements in Article 33 of EMIR as well as relevant additional requirements (e.g. derived from the German Stock Corporation Act or the Banking Act). Therefore, it is very important that the Guidelines on CCP conflicts of interest management do not conflict with already existing rules and allow a risk-based approach, consistent with existing rules for credit institutions.

While we generally agree with the proposals made by ESMA, we see the need for certain adjustments or clarifications. In the following, we have put our remarks in this regards into our answers to the questions below.

C. Comments to Questions

Q1. Do you agree with the definition and with the scope here above described?
Eurex Clearing response: Eurex Clearing agrees with the definition and scope of conflicts of interest to the extent that these conflicts are affecting the interests of the CCP and therefore, are manageable by the CCP. Conflicts of interest that do not affect interests of the CCP should be excluded from the scope. In particular, the guidelines include the relationship between clearing members, clients or between a clearing member and a client as a potential source of conflicts of interest, which should be considered by the CCP. We have strong concerns to address / consider potential conflicts of interest between these parties in the CCPs conflicts of interest management, especially if they are not associated with the business of the CCP. In accordance with current EMIR requirements, clients can either be disclosed or undisclosed to the CCP. Undisclosed clients are only known to their clearing member. Hence, a CCP cannot be aware of all conflicting interests between a clearing member and the undisclosed clients. Furthermore, undisclosed clients could influence interests of the clearing member, which then would not be transparent to the CCP.

In addition to this lack of information, a CCP has no legal basis to manage conflicts of interest between clearing members, clients or between a clearing member and a client.

For all conflicts of interest that do not affect the interests of the CCP, clearing members and clients should primarily be self-responsible to identify and manage their conflicts of interest with other clearing members or clients. Therefore, we propose to delete this requirement from paragraph 19.

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

Eurex Clearing response:

Eurex Clearing proposes a more flexible approach within the guidelines to avoid an inappropriate use of confidential information.

Paragraph 23 requires that a specific confidentiality agreement should be signed by staff members and clearing members involved in the risk committee and in the default management groups. We agree that there should be strict confidentiality obligations for these parties and we agree that a CCP should ensure that these confidentiality obligations are known by and apply to all involved parties. However, we do not see the need to sign specific confidentiality agreements, if existing provisions (e.g. terms of reference) already cover all relevant confidentiality obligations.

Therefore, we propose to emphasize the need that staff members and clearing members involved in the risk committee and in the default management groups should be subject to strict confidentiality obligations but allow a more flexible approach on how to reach this requirement.

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

Eurex Clearing response:

Eurex Clearing considers the proposed rules of conduct as appropriate, but recommends to consider already existing requirements.

Regarding the rules related to the limitation of the number of contracts or mandates board members and executive directors may have, we propose to clarify the rules by including specifications on the required limitations. These limitations should not conflict with currently existing rules for credit institutions, which already determine specific qualitative requirements as well as concrete limitations of the number of mandates for management bodies (i.a. Article 91 (3) in Directive 2013/36/EU).

For potential conflicts of interest with external auditors, there are already sufficient requirements in Regulation (EU) No 537/2014 and transpositions into national law in place. These requirements specify forbidden activities that are conflicting with their activities as the external auditor. In order to prevent misinterpretations of the term "external audits having a link with or receiving benefit from the CCP" we propose adding a reference to the existing rules or deleting this specific requirement.

Q4. Do you believe that the CCPs should apply such rules concerning the gifts?
Eurex Clearing response: Eurex Clearing welcomes the proposed rules concerning the gifts.

Q5. Are you in favour that CCPs should adopt the above clear rules on the ownership of the financial instruments?
Eurex Clearing response: Eurex Clearing welcomes the approach to define clear rules on the ownership of the financial instruments. Nevertheless, these rules should first of all focus on specific dangers of conflicts of interest and further more respect the right of data protection. This affects especially the rules regarding the pre-approval process and the portfolio disclosure. A CCP should be able to determine on a risk-based approach, for which department or staff a pre-approval request for specific financial instruments appears necessary. Only areas with a potential vulnerability for these kinds of conflicts should be in scope of the approach. The specific threats to enter into a conflict of interest based on the ownership of financial instruments only applies to few employees. Furthermore, restrictions for specific financial instruments in certain situations (e.g. during an ongoing acquisition) are more effective and efficient than a pre-approval process. Thus, the pre-approval process should only be one option rather than a mandatory approach. A disclosure of the financial instruments portfolio for staff members may be seen as a strong intrusion into their privacy and should be considered with great care on a sensitive weighing of interests. A core data protection principle is the necessity of personal data for a legitimate reason. Disclosure obligations for every employee will in many cases cross the border of appropriateness. Further restrictions could result from different affected labour law regulation and jurisdictions. In our experience, only selected categories of personnel face risks for potential conflicts of interest based on their portfolio. Thus, a portfolio disclosure requirement for all staff members appears not proportionate. The Guidelines do not explain the specific nature of the risk that is to be mitigated in this regard, but we presume that there is an assumption that an individual CCP employee's action could be influenced by the impact, e.g., on a clearing member in which the employee has a financial interest. Such general risk, however, should already be substantially mitigated by an effective implementation of the CCP's applicable rules and regulations. Furthermore, paragraph 26 already requires to disclose all (potential) conflicts of interest and thus allows the CCP to take measures to avoid the conflicting situation. In addition, the detection of actual conflicts of interest can be reached through a transaction-based monitoring process. In our opinion, it is more important to sensitize all staff members regarding potential areas, which could lead to a conflict of interest. Therefore, we recommend to exclude the portfolio disclosure requirement from paragraph 31 or to allow the CPP to limit the disclosure to specific financial instruments, specific persons or determined thresholds of financial instruments on a risk-based approach.

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?
Eurex Clearing response: Eurex Clearing fully supports the requirement to train CCP staff appropriately on the applicable law and policies concerning conflicts of interest on a regular basis.

Q7. Do you agree on the above-proposed rules?
Eurex Clearing response: Eurex Clearing proposes a more comprehensive approach. In its responsibilities to oversight the compliance function, the CCP's board should rather monitor the effectivity of the CCP arrangements to prevent and manage the conflicts of interest, than the efficiency of it. An efficient way to prevent and manage conflicts of interest could be an indicator to assess the effectivity of the process, but should not be the only aspect under consideration.

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?
Eurex Clearing response: Eurex Clearing agrees to most of the organisational arrangements referring to a CCP itself, but firmly disagrees to the rules affecting entities, which are not controlled by the CCP. In order to avoid duplicative or potentially conflicting requirements, we would recommend to appropriately consider the governance models mandated under the national company law in Europe, and ensure that the provisions in the guidelines are compatible with the legal framework in the various member states. This affects especially the requirements outlined in paragraph 39 and 40. The requirement that a CCP should be well-represented and in a balanced manner at the level of board of the mother company, conflicts with the German Stock Corporation Act (AktG). The AktG determines that only the Supervisory Board of a company in its sole discretion can appoint the Executive Board. The same applies to the nomination of candidates by the Supervisory Board and the election of the members of the Supervisory Board by the shareholders' meeting. Finally, the AktG only provides for shareholders to designate members directly to the Supervisory Board. Therefore, a subsidiary has no legal basis to influence decisions regarding the board of the mother company. This also applies for the rules outlined in paragraph 40. A subsidiary cannot influence the definition of roles for the board of the mother company or other companies it does not control. We propose to limit requirements for organisational arrangements to the level of the CCP.

In addition to the described conflict with the AktG, we see a potential conflict with the limitation requirement for the number of contracts or mandates board members may have as outlined in paragraph 26. In our understanding, the objective of paragraph 26 is to ensure that board members can focus on their work for the CCP, while paragraph 39 requires that board members are part of several boards within a group to represent the interests of the CCP appropriately.

Furthermore, we recommend to exclude the requirement to define penalties for outsourcing agreements within the same group as outlined in paragraph 49. Fixed penalties could lead to a weakened environment for the prevention of conflicts of interest due to additional pressure. The need to fulfil outsourcing agreements is sufficiently covered by determined reporting requirements, along with appropriate escalation and enforcement mechanisms.

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

Eurex Clearing response:

Eurex Clearing considers the described procedures as appropriate, but sees the need for clarification of the following terms:

Referring to paragraph 55, the term "sufficient independence" in the context of the decision-making process is not specified. In general, we would consider all persons not directly involved in the conflict of interest as sufficiently independent. Therefore, we propose to clarify the term "sufficient independence" in that manner. Further, it should be complemented that in case of doubt, a joint decision by different persons or bodies may be considered necessary to reach an objective decision making process for the conflict of interest.

Referring to paragraph 56, it should be made clear that not all of the listed measures to remedy probable or existing conflicts of interest are mandatory. The measures taken should be based on a risk-based approach.

Referring to paragraph 59, the term "material breaches" should be specified to reach a consistent approach for the reporting requirements to the competent authority. Furthermore, the described timeline to report material breaches to the national competent authority should only start after the breach has been recognised and analysed to a reasonable extend.

Referring to paragraph 60, the conflict of interest register should be aligned with current market standards for credit institutions. This affects especially the need to track and record trainings performed by the staff and received gifts, which is required in paragraph 60 but not in line with current market standards for credit institutions in our experience.