CME Group

January 17, 2020

**VIA ELECTRONIC SUBMISSION**

European Securities and Markets Authority
201-203 Rue de Bercy
75012 Paris
France

**Re: Consultation Paper on Procedural rules for penalties imposed on Third-Country CCPs, TRs and CRAs**

To Whom It May Concern:

CME Group Inc. ("CME Group"), the parent of Chicago Mercantile Exchange Inc. ("CME"), a derivatives clearing organization ("DCO") registered with the U.S. Commodity Futures Trading Commission ("CFTC"), appreciates the opportunity to comment on the European Securities and Markets Authority's ("ESMA") consultation paper on *Procedural rules for penalties imposed on Third-Country CCPs, TRs and CRAs* ("the Consultation Paper").[1] CME's clearing house division offers clearing and settlement services for exchange-traded futures and options on futures contracts, as well as certain swaps, including interest rate swap products.

CME Group continues to believe, as it has noted in responses to other consultation papers published by ESMA and the European Commission,[2] that the European Union ("E.U.") should adopt a policy of mutual regulatory deference with respect to the oversight of non-E.U. based central counterparties ("CCPs"). For decades, such a policy, including as implemented by the CFTC for non-U.S. exchange-traded derivatives, has allowed market participants around the world to efficiently hedge their business risk. It also supports efficient markets by generating deep pools of liquidity, encouraging efficient price discovery, and reducing market fragmentation. Further, an approach of mutual regulatory deference allows a CCP's home country regulator to adopt and apply regulatory requirements that are tailored to the unique characteristics of the markets it oversees, while recognizing that one jurisdiction's requirements are on an outcomes-basis comparable to another jurisdiction's requirements.

---

1 ESMA, *Consultation Paper*, *Procedural rules for penalties imposed on Third-Country CCPs, TRs and CRAs* (Dec. 2019), *available at* https://www.esma.europa.eu/sites/default/files/library/esma43-370-12_ta_cp_on_ccp_penalties.pdf.

2 CME Group Inc., Letter in response to ESMA consultation papers on *Draft technical advice on criteria for tiering under Article 25(2a) of EMIR 2.2* (July 2019), *available at* https://www.esma.europa.eu/press-news/consultations/draft-technical-advice-criteria-tiering-under-article-252a-emir22; CME Group Inc., Letter in response to ESMA consultation report on *Technical Advice on Comparable Compliance under Article 25a of EMIR* (July 2019), *available at* https://www.esma.europa.eu/press-news/consultations/technical-advice-comparable-compliance-under-article-25a-emir; and Sunil Cutinho, President CME Clearing, Letter to Valdis Dombrovskis, Vice-President for the Euro & Social Dialogue, European Comm'n (Oct. 2017) (responding to EMIR 2.2. proposal), *available at* https://ec.europa.eu/info/law/better-regulation/initiatives/com-2017-331/feedback/F7443_en?p_id=30988.



20 South Wacker Drive Chicago, Illinois 60606 T 312 930 1000 F 312 466 4410 cmegroup.com

EMIR 2.2 revises the legal framework under which non-E.U. CCPs are recognized in the E.U. Under this new framework, ESMA is provided express powers to impose fines and penalty payments on non-E.U. CCPs. Consistent with our views on mutual regulatory deference, we continue to believe that direct supervisory and enforcement authority should be left to a CCP's home country regulator. This approach is prudent and efficient and will ensure that the regulator with the strongest interest and expertise with respect to the CCP is the final arbiter of CCP supervision and enforcement. To the extent that such an approach is not followed, we believe, at a minimum, that the home country regulator should be consulted in advance of any potential disciplinary action by a foreign regulator.

Non-E.U. CCPs are legal entities established outside of the E.U. that have not established separate legal entities in the jurisdiction of the E.U. in order to provide clearing services to customers in the E.U. Instead, customers established in the E.U. have made an independent business decision to leave the jurisdiction of the E.U. and come to the jurisdiction of the non-E.U. CCP in order to hedge their business risk in markets cleared by the non-E.U. CCP. E.U. legislators and ESMA have chosen to expand their jurisdiction beyond the E.U. by following customers established in the E.U. into jurisdictions outside of the E.U. We strongly believe that this distinction is important in contemplating the appropriate procedural protections that should be put in place for non-E.U. CCPs' potential fines and penalty payments, particularly those related to urgent actions.

Furthermore, as discussed below (see discussion and table under *Inappropriateness of ESMA's Powers for Non-E.U. Financial Market Infrastructures),* this distinction is also the reason that ESMA's rules of procedure on fines and periodic penalty payments imposed on EMIR-registered Trade Repositories are not an appropriate model for the levying of fines and periodic penalty payments on non-E.U. CCPs. Unlike EMIR-registered Trade Repositories, which have established legal entities in the jurisdiction of the E.U., non-E.U. CCPs have not established separate legal entities in the jurisdiction of the E.U. Any authority to levy penalties and fines on such non-E.U. entities, particularly with respect to urgent actions, should be subject to robust and significant due process protections, with specific requirements to consult with the home country regulator for these non-E.U. CCPs.

While we have broad concerns with ESMA's powers to fine and impose penalty payments on non-E.U. CCPs, we are particularly concerned with such powers in the context of non-E.U. CCPs that have been deemed systemically important to the E.U. (i.e., "Tier 2 CCP"). Under EMIR 2.2., non-E.U. CCPs are required to comply with the majority of domestic regulations for E.U. CCPs and in turn, non-E.U. CCPs may be subject to fines and/or penalty payments for failing to comply with (i.e., infringing) such regulations. This is particularly concerning where an inappropriate approach is employed under EMIR 2.2. for determining if a non-E.U. CCP is systemically important, as is proposed by ESMA. Where this occurs, a Tier 2 CCP with a *de minimis* nexus to the E.U. could be subject to fines and penalty payments relating to its compliance with E.U. regulatory requirements, to which it should not be subject in the first place. This predicament is even more egregious because ESMA has not proposed a true comparable compliance framework. As a result, a Tier 2 CCP could be subject to fines and penalty payments for infringing E.U. regulatory requirements even where it complies with domestic requirements that on a outcomes-basis are comparable to E.U. regulatory requirements.

In addition to these substantive concerns with the fining authority in EMIR 2.2, we have outlined our primary procedural concerns with the proposed fines and penalty payment framework in the Consultation Paper below.



20 South Wacker Drive Chicago, Illinois 60606 T 312 930 1000 F 312 466 4410 cmegroup.com

**Specific Comments**

*ESMA's Procedures for Fines & Penalty Payments Should Require Consultation with Non-E.U. CCPs' Home Country Regulators*

Under EMIR 2.2., ESMA would be able to impose significant fines and penalty payments on a non-E.U. CCP—e.g., up to 20% of its annual revenue—regardless of whether the CCP is systemically important. While these powers are inherently concerning, the Consultation Paper includes no requirement that ESMA consult with a non-E.U. CCP's home country regulator with respect to a decision or fine, contrary to principles of mutual regulatory deference and international comity. To the extent ESMA can impose fines and penalty payments on a non-E.U. CCP, a non-E.U. CCP's home country regulator should be consulted in advance of any fines or penalty payments being issued. A CCP's home country regulator must be the primary supervisor of the CCPs domiciled in its jurisdiction. Providing ESMA with the unilateral ability to impose fines and penalty payments directly conflicts with such primary supervision and could have negative implications for the efficient functioning of global financial markets.[3] A home country regulator consultation requirement could mitigate the likelihood of such an outcome.

*ESMA's Urgent Action Authority Should Require Consultation with Non-E.U. CCPs' Home Country Regulators and Provide Greater Transparency to Non-E.U. CCPs*

The Consultation Paper proposes in its procedure for interim decisions that "[w]here there is cogent and consistent evidence that an urgent action by ESMA is needed in order to prevent significant and imminent damage to the financial system," ESMA may take action to issue a decision against and fine a non-E.U. CCP without even considering a response from the CCP. While CME Group is inherently concerned with the ability of any regulator to impose fines on a CCP without due process, the vague requirements proposed for taking such action in the Consultation Paper and lack of consultation with the non-E.U. CCP's home country regulator are particularly problematic. Beyond the lack of standards to define what constitutes "cogent and consistent evidence," or what circumstances would constitute "significant and imminent damage," the Consultation Paper provides no safeguards that would prevent ESMA from effectively directing a non-E.U. CCP to stop or change its practices in a manner that would conflict with the guidance or direction that the CCP receives from its home country regulator.

A requirement to consult with a home country regulator when urgent action against a non-E.U. CCP is contemplated would serve to mitigate this risk. Unfortunately, as written, the Consultation Paper allows for a situation to occur in which a non-E.U. CCP may be forced to choose between complying with a requirement or direction of its home country regulator and one sought to be imposed by ESMA. CCPs—and, by extension, the customers and markets they serve—must not be placed in this position, particularly if effectively failing to follow ESMA's directive exposes a CCP to significant fines.

Beyond this significant risk, the Consultation Paper's proposed procedure for taking interim decisions to impose fines or penalty payments is lacking in due process. ESMA does not explain

[3] The Commodity Exchange Act specifically requires the CFTC to consider, among other factors, "whether the amount of [a] penalty [imposed upon a registered entity, including a Derivatives Clearing Organization] will materially impair the ability of the registered entity to carry on its operational duties." 7 U.S.C. § 13a. This places the focus of the CFTC's enforcement authority on encouraging and allowing for remediation (rather than imposing fines so punitive that a CCP is forced to wind down its operations), and allows the CFTC to adequately sanction CCPs for statutory and rule violations while preventing undue harm to the customers and markets that they serve.



20 South Wacker Drive Chicago, Illinois 60606 T 312 930 1000 F 312 466 4410 cmegroup.com

these apparent shortcomings. For example, the Consultation Paper proposes that an investigation officer issuing findings related to urgent action only shall "inform the person subject to the investigation" of the findings and provide a statement of findings. However, it is unclear why ESMA believes the person subject to those findings should not be allowed to make submissions to the investigation officer of any sort, or even access the file related to the findings, which would provide a measure of transparency to the process at little cost or risk. We believe it critical that, in addition to consultation with the home country regulator, due process is afforded in a manner consistent with the tenets of the legal regime in which the non-E.U. CCP is located.

*ESMA's Procedures for Fines & Penalty Payments Should Clearly Allow Non-E.U. CCPs to Make Use of Outside Experts, including Home Country Regulators, and Testimony*

The Consultation Paper provides that a person who is the subject of an investigation may make written submissions and be assisted by "their lawyers or other qualified persons admitted by the investigation officer." However, ESMA does not explain the standards investigation officers will use to determine who is a "qualified person," and the Consultation Paper does not specify whether written submissions and testimony from outside experts, including representatives of a non-E.U. CCP's home country regulator, would be allowed. For reasons stated above, particularly where a non-E.U. CCP's home country regulator is not required to be consulted, submissions and testimony by such individuals could prove critical to ensuring that action taken by ESMA does not unduly impair a non-E.U. CCP's ability to carry on its business, potentially harming customers and impairing the function and operation of the markets it serves.

*ESMA's Procedures for Fines & Penalty Payments Should Be Clearer With Respect to the Mechanism for Limiting Periods for the Imposition and Enforcement of Penalties*

Under the Consultation Paper, while ESMA's ability to impose fines and periodic penalty payments would be subject to a limitation period of five-years, "[a]ny action taken by ESMA for the purpose of the investigation or proceedings in respect of an infringement" would "interrupt the limitation period," and each interruption would start the limitation period anew. The Consultation Paper does not specify whether the limitation period for one infringement can be tolled and restarted based on action taken by ESMA related to an investigation or proceeding for a separate infringement. The Consultation Paper should at a minimum specify that an action taken by ESMA for the purpose of the investigation or proceedings related to an infringement would interrupt and restart the limitations period *only* as to the infringement that is the subject of the action or proceedings. Similarly, with respect to ESMA's proposed limitations period for the enforcement of penalties, ESMA proposes that the eight-year period to enforce decisions may be interrupted and start anew based on "a notification by ESMA to [a non-E.U. CCP] . . . of a decision varying the original amount of the fine or periodic penalty payment." To the extent ESMA is able to unilaterally adjust the amount of a fine or periodic penalty payments,[4] eliminating this condition with respect to when the period to enforce decisions may be interrupted and restarted would ensure that decisions to vary fines or periodic penalty payments are not driven by the purpose of increasing the time available to enforce penalties.

---

[4] Recital 48 and Article 25g of EMIR 2.2 provide that with respect to fines, ESMA should set a basic amount and adjust, if necessary, by certain coefficients outlined in Annex IV, some of which are qualitative in nature (*e.g.*, "if the CCP's senior management has not cooperated with ESMA in carrying out its investigations, a coefficient of 1.5 shall apply"). Article 25h of EMIR 2.2 provides that a periodic penalty payment "shall be imposed for a maximum period of six months following the notification of ESMA's decision," and "[f]ollowing the end of the period, ESMA shall review the measure."

*(cont'd)*



20 South Wacker Drive Chicago, Illinois 60606 T 312 930 1000 F 312 466 4410 cmegroup.com

*Inappropriateness of ESMA's Powers for Non-E.U. Financial Market Infrastructures*

Beyond CME Group's comments above relating to more technical procedural items, in proposing these procedures in the Consultation Paper, ESMA has acknowledged that it sought to replicate the Trade Repositories Commission Delegated Regulation[5] with regard to the rules of procedure on fines and periodic penalty payments imposed on EMIR-registered Trade Repositories. Yet there is a fundamental difference between the levying of fines and periodic penalty payments under that regulation and the levying of fines and periodic penalty payments in the case of non-E.U. CCPs, as illustrated in the following table, which distinguishes the rationality of ESMA having unilateral fining authorities for E.U. domiciled Trade Repositories from the inappropriateness of ESMA having such powers for non-E.U. CCPs:

| **E.U. Trade Repository** | **Non-E.U. CCP** |
|---|---|
| E.U. legal entity | Non-E.U. legal entity |
| Market infrastructure enters E.U. market to provide services to E.U. customers | E.U. customers leave E.U. market to access global markets |
| Majority E.U. customers | Majority non-E.U. customers |
| Primary supervisor is ESMA | Primary supervisor is non-E.U. regulator |
| **Appropriate outcome:** ***Unilateral fining powers by ESMA*** | **Appropriate outcome:** ***Unilateral fining powers by home country regulator (or at minimum consultation of home country regulator before fining by ESMA)*** |

We note that ESMA does not have powers to levy fines or periodic penalty payments in the case of non-E.U. trade repositories that have been recognized by ESMA. CME Group agrees with this approach, which aligns with a policy of mutual regulatory deference. Therefore, we strongly urge European policy-makers to adopt for non-E.U. CCPs the same approach they took for non-E.U. trade repositories with respect to fines and periodic penalty payments.

Trade Repositories registered under EMIR are firms that have established legal entities in the jurisdiction of the E.U. in order to actively provide trade reporting services to customers in the E.U. By contrast, non-E.U. CCPs are legal entities established outside of the E.U. that have not established legal entities in the jurisdiction of the E.U. in order to provide clearing services to customers in the E.U. Instead, customers established in the E.U. have made an independent business decision to leave the jurisdiction of the E.U. and come to the jurisdiction of the non-E.U. CCP in order to hedge their business risk in markets cleared by the non-E.U. CCP. E.U. legislators, and ESMA, have chosen to expand their jurisdiction beyond the E.U. by following customers established in the E.U. into jurisdictions outside of the E.U. We strongly believe that this distinction is important in contemplating the appropriate procedural protections that should be put in place for non-E.U. CCPs' potential fines and penalty payments, particularly those related to urgent actions. In particular, this distinction calls for robust and significant due process protections with specific requirements to consult with the home country regulator for these non-E.U. CCPs.

[5] Commission Delegated Regulation (EU) No 667/2014 of 13 March 2014 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to rules of procedure for penalties imposed on trade repositories by the European Securities and Markets Authority including rules on the right of defence and temporal provisions, OJ L 179, 19.6.2014, pg. 31.



20 South Wacker Drive Chicago, Illinois 60606 T 312 930 1000 F 312 466 4410 cmegroup.com

CME Group

**Conclusion**

CME Group continues to have significant concerns regarding the ability of ESMA to fine and impose penalty payments on non-E.U. CCPs. These concerns are heightened by the proposals in the Consultation Paper that allow ESMA to take such actions without consulting the non-E.U. CCP's home country regulator. The ability to take such actions without consultation runs counter to the spirit and principle of mutual regulatory deference and international comity and we strongly urge that enhanced due process and procedural protections be put in place for non-E.U. CCPs.

CME Group appreciates the opportunity to comment on this matter. We would be happy to discuss any of the topics raised in our response further. If you have any comments or questions, please feel free to contact me, or Simon Turek, Senior Director, Government Relations at simon.turek@cmegroup.com.

Sincerely,

Sunil Cutinho
President, CME Clearing
Chicago Mercantile Exchange, Inc.
20 South Wacker Drive
Chicago, IL 60606