EACH

European Association of CCP Clearing Houses

EACH response to the ESMA consultation on the methodology for calculation and maintenance of the additional amount of pre-funded dedicated own resources (Article 9(15) of CCPRRR)

September 2021

Introduction

The European Association of CCP Clearing Houses (EACH) represents the interests of Central Counterparties (CCPs) in Europe since 1992. CCPs are financial market infrastructures that significantly contribute to safer, more efficient and transparent global financial markets. EACH currently has 19 members from 15 different European countries. EACH is registered in the European Union Transparency Register with number 36897011311-96.

EACH appreciates the opportunity to provide feedback to the ESMA Consultation Paper "Draft RTS on the methodology for calculation and maintenance of the additional amount of pre-funded dedicated own resources (Article 9(15) of CCPRRR)" (hereinafter called "The consultation").

Section 4.1 – General considerations – basic elements of the methodology

Question 1: Do you agree with the proposed approach to define the basic elements of the methodology for the calculation and maintenance of the additional amount of pre-funded dedicated own resources? If not, please explain why and how you would suggest changing the basic elements of the formula?

EACH generally agrees with the basic elements for the calculation and maintenance of the additional amount of prefunded dedicated own resources, i.e. the "second skin in the game" (SSITG).

EACH particularly welcomes that ESMA follows the advice in Level 1 to calculate the SSITG as a percentage of the CCP's risk-based capital. This is particularly important to support a proportionality approach that caters for the actual risk born by CCPs, rather than making them subject to minimum levels of own funds beyond risk-based calculations. While this provision of the level 1 text would particularly affect some smaller CCPs, we believe that it is also important that the level 2 text also ensures a proportionality approach. This should avoid that CCPs that have posed no risk concerns based on the ongoing supervision or the regular ESMA stress tests, are unduly subject to higher own resources requirements.

There are a few aspects of the proposed methodology that, in our opinion, require some **clarifications in line with the points above**:

1. As detailed further in our response, it appears to EACH that certain indicators included in Table 1 "Summary of proposed parameters" of the consultation seem to **penalize CCPs for practices they are authorized to perform under EMIR** and for which they are already **duly supervised**, for instance clearing more than one currency, participating in interoperability arrangements, etc. In addition, the proposed

methodology also includes indicators related to the topic of the robustness of the CCP's risk management framework, which is already dealt with in the EMIR RTS. EACH would like to **caution against regulating the same topic in two different regulatory contexts** (EMIR and CCP Recovery and Resolution (CCP RR)) as this can lead to significant legal uncertainty, considering that the two regimes may be supervised by different authorities and may diverge over time.

2. The sum of all the maximum indicators' value included in Table 1 amounts to **45% of the CCP's risk-based capital**, i.e. **much higher than the maximum of 25% of the CCP's risk-based capital** foreseen in the CCP RR Level 1 Regulation[1]. This considerably increases the possibility that CCPs will have to dedicate 25% of their risk-based capital, while, to our understanding, the objective of the Level 1 Regulation is to allow for a more **proportionate approach** in line with ESMA's note under paragraph 22 of the consultation paper. We therefore suggest in our response to remove certain indicators that e.g. do not seem to be in line with the Level 1 text or, as mentioned above in point 1, would lead to **penalizing CCPs** for performing practices they are **authorized to perform under EMIR**.
3. In addition to the general approach to calculate the SSITG, we would like to caution against the burdensome maintenance process. ESMA suggests that every time one of the parameters of the calculation of the formula is modified, CCPs have to review and re-calibrate their SSITG. Some of the parameters may need minor updates in daily operations of a CCP, for example in relation to staffing levels or exposures in terms of collateral contributions. A recalibration of the SSITG **whenever one of the parameters of the calculation formula is modified and at least on a yearly basis – as detailed in paragraph 17 of the consultation[2] – would therefore result in an extensive operational burden for CCPs**. EACH would suggest a **review of the SSTIG only on a yearly basis,** therefore **deleting the sentence "and each time the percentage level evolves after conducting a review in accordance with paragraph 2" in Article 1(4) of the draft RTS.** It would indeed not be recommendable to review the SSITG more frequently than the "first" SITG, as the former, being placed basically at the bottom of the default waterfall, is less likely to be employed than the latter. A calibration of the SSIG on a yearly basis, rather than every time a parameter changes, would not only adequately capture significant changes in a CCPs' risk profile but also ensure that the SSTIG is adequate and incentivizes proper risk management, but also be in line with the timeframe established by EMIR for the review of the "first" SITG.

Table 1: Estimated amount of SSITG per CCP according to the methodology proposed by ESMA

CCP	Estimated amount of SSITG (% of the CCP's risk-based capital)
CCP 1	10%
CCP 2	Between 13.5% and 16.5%

[1] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021R0023&from=EN

[2] *Frequency of the review: the minimum amount of additional prefunded resources shall be revised every time the CCP's capital requirements are revised or each time one of the parameters of the calculation formula is modified, and at least on a yearly basis*

CCP 3	16.8%
CCP 4	17%
CCP 5	19.3%
CCP 6	20%
CCP 7	Between 19.5% and 20%
CCP 8	21.4%
CCP 9	24%
CCP 10	25.5 % +- 2%
CCP 11	25%

Table 1 above shows the estimated amount of SSITG per CCP calculated by EMIR authorized EACH Members according to the methodology proposed by ESMA. As we can see, only one CCP estimates to dedicate an amount of SSITG of 10% while the majority of estimates are closer to 25%. EACH does **not believe this ensures the proportionality** that, as mentioned above, we understand is one of the purposes of the Level 1, especially considering that:

- CCPs are already **complying with the very stringent EMIR requirements** and often go even beyond EMIR to be as conservative as possible;
- At **international level** it is very unusual to have a "first" level of required SITG, let alone a second.

As a final observation, we would like to underline that the SSITG should not be seen by clearing members as a guarantee for risk taken on by them. CCPs should continue to be a neutral party interposed between a buyer and a seller but should not have to cover risks entered into by the counter parties. The risk management systems of CCPs are conceived in such a way that those who create risk exposures back these up with sufficient collateral. The SSITG needs to be calibrated so it fulfils its role and not to incentivize inappropriate risk taking by the clearing members.

Section 4.2 – Methodology for determining the appropriate % level of SSITG

Question 2: Do you agree with the schematic formula combining a set of parameters assessed by the CCP? If not, please explain why and how you would suggest changing the formula?

EACH agrees with the schematic formula combining a set of parameters assessed by the CCP. However, we would like to reiterate that, as mentioned in our response to Question 1, we see the need to clarify why the **sum of all the maximum indicators values** included in Table 1 amounts to **45% of the CCP's risk-based capital**, i.e. **much higher than the maximum of 25% of the CCP's risk-based capital** foreseen in the CCP RR Level 1 Regulation. This approach would thwart the principle of proportionality that was preserved in the Level 1 text, according

to which small CCPs with few business lines and lower risk-profile should not maintain much higher second SITG as the 10% of its risk-based capital.

Question 3: Do you agree with the list of parameters to describe the structure and the internal organisation of CCPs and the nature, scope and complexity of a CCP's business? If yes, are there additional parameters that should be added to the list? If not, please explain why and how you would suggest assessing the internal organisation of CCPs and the nature, scope and complexity of a CCP's business in the methodology?

EACH has a few observations to put forward regarding the list of parameters and **indicators** to describe the structure and the internal organisation of CCPs and the nature, scope and complexity of a CCPs' businesses:

1. **Parameter A1 – "*Nature and complexity of the asset classes cleared*"**
   As a general comment, we would like to suggest including **thresholds** in cases where volumes of a specific asset cleared are negligible. We do not think that allocating 1% per asset class is recommendable if volumes in that particular asset class pose a negligible additional risk to its participants and the EU market. The following specific comments are made on several of the indicators under Parameter A1:
   a. **Indicator "*Are there more than one asset class under the same default fund?*"**– EACH is of the opinion that the formula to calculate the SSITG should be **neutral**, and not try to favour one model (i.e. having only one asset class per default fund) over the other (i.e. having more than one asset class per default fund), since both types of models are subject to supervisory approval. EACH therefore suggests **removing this indicator**.
   b. **Indicator "*Does the CCP clear assets denominated in or offer settlement in more than 1 currency?*"** – EACH believes that as long as the CCP is authorized under EMIR to clear specific currencies and has in place the adequate risk management procedures to manage more than one currency, it should not be penalised via CCP RRR by requiring it to dedicate a higher amount of SSITG, also considering that clearing more than one currency is an extremely **common and well established practice among CCPs** and it does not refer only to a small minority. EACH therefore suggest **removing this indicator**.
   c. **Indicator "*Does the CCP clear assets denominated in or offer settlement in at least 1 non-EU currency*?"** – We respectfully believe that this indicator can be considered as duplicative compared to the above-mentioned indicator "*Does the CCP clear assets denominated in or offer settlement in more than 1 currency?"*, and therefore **EACH suggests deleting it.**
   d. **Indicator "*Does the CCP offer physical settlement of derivatives contracts?*"** – EACH is of the opinion that it is not appropriate to differentiate between physical settlement of derivative and commodities derivative products and allocate a further 1% per each category, due to the complexities involved in differentiating between commodities. For instance, a CCP physically setting

commodity derivatives (e.g. Agricultural Futures) will be assigned 2% score, (1% for parameter A1.5 and 1% for parameter A1.6). There is a lack of independence between the two indicators which will bias the result for some CCPs. An **alternative proposal** would be to **keep this indicator** and **remove the one on settlement of commodities derivatives contracts (A1.6)**.

EACH suggests looking at the **type** of asset classes rather than the number, as well as at the **number of processes** to clear the instrument and to default manage it (e.g. calculation of IM, calculation of VM, cascading process of rolling over futures, adapting the algorithm to determine the fixing price, physical delivery, etc). In addition, EACH would like to clarify that by "asset classes" we refer to the ones proposed by ESMA in the **ESMA 2021 CCP Stress Test Instructions document**[3].

2. **Parameter A2 – "*Scope and complexity of the CCP's activities*"**
    a. **Indicator "*Do clearing members established outside the EU represent more than 20% of the CCP's clearing membership (by collateral)?"*** – **EACH suggests deleting this indicator** because, according to EMIR Art. 37.1 "*Participation requirements*"[4] the CCPs are obliged to establish admission criteria that are non-discriminatory, transparent and objective in order to ensure fair and open access to CCPs. Penalizing the CCP for accepting non-EU clearing members would therefore **conflict with this non-discriminatory principle**.
    b. Indicator *"**Do the top 5 clearing members of the CCP represent more than 40% of the CCP's prefunded resources (aggregated across all services and default funds)?"*** – EACH is of the opinion that, for the sake of legal certainty, it is required to define the frequency and the timeframe of the calculation of the top five clearing members' representation. EACH suggests the calculation to be performed on a **yearly basis**, in line with our suggestion on the frequency for the review of the SSITG as well as with the review of the "first" SITG as per EMIR dispositions.
    c. **Indicator "*Does the CCP participate in an interoperability arrangement?*"** – As a first comment, we would like to underline that the CCP's "first" SITG is to be used only in case of default of one or more clearing members, and **not for interoperability arrangements** therefore we do not see the reason to add 2% to the SSITG if the CCP participates in an interoperability arrangement.

       In addition, CCPs already have robust risk management procedures in place to cover any risks that may arise from interoperability arrangements, and where a

[3] Asset classes: Equities and ETFs; Bonds and repo positions; Equity derivatives; Commodity derivatives and warrants; Fixed; Income derivatives; Credit derivatives; Freight derivatives; Emission allowances; FX derivatives; Structured finance products; ETC and ETN bond types; Securitised derivatives; Contracts For Differences; Volatility Index; Derivatives; Dividend Index derivatives; Forward starting repos; Cross-currency swaps and derivatives; Inflation Derivatives.

[4] A CCP shall establish, where relevant per type of product cleared, the categories of admissible clearing members and the admission criteria, upon the advice of the risk committee pursuant to Article 28(3). Such criteria shall be non-discriminatory, transparent and objective so as to ensure fair and open access to the CCP and shall ensure that clearing members have sufficient financial resources and operational capacity to meet the obligations arising from participation in a CCP. Criteria that restrict access shall be permitted only to the extent that their objective is to control the risk for the CCP.

CCP has been authorized under EMIR to participate in such arrangements, it should not be penalized. Generally, penalizing interoperability arrangements will discourage CCPs from participating into one/continuing participating in one. This will directly annihilate the positive effects of interoperability arrangements observed where interoperability arrangements have been implemented for specific asset classes, notably securities transactions, which will have negative effects both on the financial stability and the recovery and resolution phase. Interoperability arrangements provide clearing members with increased opportunities for netting and lead to a reduction in outstanding gross exposures in the system, thus decreasing the systemic risk and have a positive effect on the financial stability in more than one jurisdiction. Another advantage of interoperability arrangements is that it is easier for clearing members to switch to another interoperable CCP. This feature is very useful during the recovery phase: if recovery does not seem likely, clearing members can be encouraged to move their business to another CCP. As a result, the CCP in recovery can be easier wound-down as business will naturally move away in a controlled manner. Interoperability therefore allows for an easier way of substituting the critical function of a CCP. As a consequence, the decreased likelihood of CCPs participating into or continuing to participate in an interoperability arrangement will also have a negative effect during recovery and resolution – this may in turn increase the need to use far reaching recovery/resolution measures (like VMGH) that affect multiple market participants.

Finally, it is also worth underlying that the Level 1 text, in Article 10.3(b)-ii, already takes the interoperability dimension into account by establishing that NCAs and supervisory colleges, when assessing the recovery plan of the CCP, shall take into consideration the overall impact that the implementation of the recovery plan would have on any linked FMI. **We therefore suggest deleting this indicator**.

d. **Indicator "*Does the CCP have more than 5 interdependencies with trading venues, payment systems and settlement systems?*"** - As a first comment, EACH is of the opinion that this indicator penalizes CCPs with multiple venues and payment/settlement systems. We **fail to see what CCPs could achieve** by increasing their amount of SSITG according to the number of interdependencies, let alone the fact that having more than 5 interdependencies constitutes a **common practice among CCPs**. The **benefits** of having several interdependencies are very similar to those explained for the previous indicator on interoperability, and as long as the CCP is authorized to have more than 5 interdependencies, is appropriately supervised and has in place an appropriate risk management framework, it should not be "punished". In addition, as specified in our comment on the interoperability indicator, the Level 1 text, in Article 10.3(b)-ii, already establishes that NCAs and supervisory colleges, when assessing the recovery plan of the CCP, shall take into

consideration the overall impact that the implementation of the recovery plan would have on any linked FMI. **EACH therefore suggest removing this indicator**.

3. **Parameter A3 – "*Internal organisation of the CCP*"**
    a. **Indicator "*Did the Board take more than 3 decisions over the last 3 years where the recommendation or advised position of the Risk Committee was not followed?*"** – EACH is of the opinion that the addition of 2% linked to positive feedback on this parameter should be **brought down to 1%**, as long as the decision by the Board not to follow a recommendation/advised position of the Risk Committee is backed by valid reasons. In this regard, rather than the *number* of decisions, the RTS should rather look at the **reasons** why the Board agreed not to follow a recommendation/advised position of the Risk Committee. If the justification is missing or invalid according to the views of authorities, then the additional 1% could be justified. It is also worth underlining that, in most cases, a (justified) Board's decision deviating from the advice given by the Risk Committee demonstrates the **Board's independence** and should rather be perceived as a positive attribute.
    b. **Indicator "*Percentage of staff in second line of defence risk functions (expressed as a % of total Full Time Equivalent (FTEs), including outsourced functions)*"** – In our opinion, the clear interpretation of *'outsourced functions'* is required when referring to this indicator. According to the EACH view, there are two possible ways of interpretation: (i) if the risk function were fully or partially outsourced, then the outsourced FTEs of the risk team shall be added to the total number of risk team FTEs; and (ii) all outsourcing functions of the CCP shall be added to the total number of employees of the CCP (this interpretation could raise further uncertainties). We would like to put forward a practical example in this regard: let's assume that the total number of a CCP's FTEs is 100, and that one IT function is outsourced to an outsourcing service provider with 35.000 FTEs worldwide. In absence of a proper clarification, in light of the indicator it could be intended that the CCP has a total of 35.100 FTEs. Going further, if the CCP risk team consists of 20 FTEs, the proportion defined in the indicator would be 20/35.100. As an **alternative option**, EACH would like to suggest replacing this indicator with the following:
        - ***"Does the CCP have in place the following 3 lines of defence in risk management?***
          1. Risk ownership: Day to day risk management and control It consists of functions that own and manage risks directly, e.g. those performed by the models development teams and the default management teams
          2. Risk control: Functions that develop, maintain and ensure compliance with risk management policies and methodologies

> ***3. Risk assurance: Functions that via internal audit provide independent assurance that risk management is working effectively; it can be performed at CCP level or, if the CCP is part of a group, at group level***"

4. **Parameter A4 – "*The robustness of the CCP's risk management framework*"**
   EACH would like to underline that this **parameter A4 does not seem to be part of the ESMA mandate under Article 9(15) of the Level 1 text** and we do not see how this could reflect the structure and internal organisation of a CCP, as well as the nature, scope, and complexity of its activities. It is also important to keep in mind that dispositions concerning the CCP's risk management framework are already dealt with in the **EMIR RTS**. In addition, we would like to highlight the following comments:
   a. For what concerns CCPs' risk management standards, these should be measured according to the **CCP's internal target when it goes above the EMIR requirements**;
   b. Increasing the level of SSITG should not be considered as a way to improve the CCP risk management, as CCPs are **already strongly incentivized** to perform robust risk management by the presence of the "**first" layer of SITG** placed in the default waterfall. The current size of the "first" SITG as included in the EMIR legislation is adequate because it is proportionate to the size of the CCP, **reflects the role of the CCP as risk manager** and is calculated on the capital that covers the risk that the CCP is responsible for. In this regard, we would like to draw ESMA's attention to the **EACH paper "*Carrots and sticks: How the skin in the game incentivizes CCPs to perform robust risk management*"**[5], whose purpose is to compare the "first" SITG to the purpose of other default management resources available at the CCP as part of its default waterfall, as well as to describe why we are of the opinion that the current calibration of SIG as included in EMIR is efficient.

   EACH therefore suggests deleting parameter A4 for the following reasons:
   a. **Indicator "*Percentage of the number of clearing services for which margins back-tests performance is below the CCP's target over the last 12 months*"** – First of all, EACH would like to make **some general comments** regarding this indicator:
      1. We respectfully believe that the indicator is **not aligned with proper risk management incentives**;
      2. Paragraph 44 of the consultation states that *"depending on the CCP's assessment, this parameter would range within **[0%;6%]**"*, while in the table the sum of the indicators value **amounts to a range [0%;8%]** – EACH would appreciate a clarification on this matter.

      While in principle, EACH acknowledges the inclusion of back-testing performance as a relevant measure, we believe that using the internal reference

[5] https://www.eachccp.eu/wp-content/uploads/2021/01/EACH-Paper-Carrots-and-sticks_How-the-skin-in-the-game-incentivises-CCPs-to-perform-robust-risk-management-January-2021.pdf

of the CCP to compute the breaches sets the wrong risk management incentive, as CCPs may be deterred from setting higher internal confidence levels compared to EMIR regulatory minimum confidence levels. In addition, using regulatory required minimum confidence levels also enhances the comparison of CCPs' risk management performance across CCPs. Also, the underlying metric and comparison lacks clarity on specification, i.e. such as the effective confidence level being below the target confidence level based on counting the number of observations, or the effective confidence level being below the target confidence level based on a statistical test - such as the Kupiec test.

Finally, the level of aggregation should be specified for which back-testing is analyzed within a clearing service, i.e. across all clearing members, at clearing member-level, or at portfolio-level. It is also worth underlining that the development of risk models falls under the EMIR supervisory procedure and **CCPs already go beyond the EMIR requirements voluntarily**, therefore they **should not be penalized** and **EACH therefore suggests deleting this indicator**.

We would appreciate if ESMA could provide **positive incentives for CCPs who voluntarily set for themselves more prudent objectives or parameters**. While CCPs already comply with the very prudent EMIR standards for risk management, some CCPs go even beyond such requirements. We therefore **suggest that for example ESMA provides for reduction of SSITG (within the 10-25% range) in case a CCP would voluntarily apply a longer MPOR than the regulatory requirement**, or set confidence level beyond 99% for their initial margin requirements (IMR). This would incentivize CCPs for even more prudent risk management, **reward those making this additional effort, while not penalizing CCPs complying with the EMIR regulation**, as such regulation is already very prudent.

It is also our understanding that certain stakeholders are advocating for the compulsory creation, within CCPs, of a **Default Management Group (DMG)** with clearing members. It is worth underlying that while some CCPs have DMGs that involve clearing members (e.g. seconded traders), CCPs should have the flexibility to decide at asset class level whether the convention of such a DMG is required. Seconded traders may or may not be needed, depending on e.g. if an order book or clear prices exists. A **flexible approach** should rather be applied in this regard, because of the potential for this to **slow decisions at a critical moment**. The time required to make a decision is particularly critical for clearing members that are bidding. The more time spent discussing the bid leaves them exposed to market moves.

b. **Indicator "*Number of days the CCP has been unable to process new trades for 1 hour or more over the last 12 months*"** – We respectfully believe that this indicator is **not in line with Article 17(6) of RTS 153/2013**, which instead foresees a **2-hour time-window in line with the recovery time objective**.

c. **Indicator "*Number of days the CCP has experienced at least one payment incident over the last 12 months, excluding incidents which are the sole responsibility of clearing members*"** – We kindly consider that the concept of **'payment incident'** is not sufficiently clear. Furthermore, we find the expression of 'the sole responsibility of clearing members' also vague, which does not support the solid interpretation of the regulation.

5. **Parameter A5 – *"Weaknesses identified by the NCA"***
   a. The term "*pending material remedial actions*" used in the consultation is quite vague and can include prudential remedial actions which can be commonly found after NCA audits or following the trigger of Article 49. These are common ongoing practices and cannot be interpreted as a measure of increased risk or instability of the CCP in question. Furthermore, the definition of a *"material weakness"* is worrisome, i.e. does "material" refer the CCP having allocated the highest materiality priority to the weakness or is it based on the NCA's own classification? All CCPs will have different metrics for determining what priority a weakness should be assigned to. Due to the lack of convergence with respect to assessing the priority of a material weakness, this will lead to unequal treatment of CCPs within the EU. Furthermore, according to Article 9(15)(a) of CCP RR Level 1, when developing the technical standards ESMA shall take into account "the structure and the internal organisation of CCPs and the nature, scope and complexity of their activities". EACH respectfully **believe that the parameter "*Weaknesses identified by the CCP's competent authority*" is not aligned with the mandate in Level 1**. This parameter de facto establishes an explicit link between compliance with regulatory requirements and CCP capital requirements, similar to the Supervisory Review and Evaluation Process (SREP) process carried out for banks by the ECB. To our understanding, as paragraphs (8), (9), (10), (11) of CCP RR Article 10 refer specifically to the assessment of recovery plans, it does not provide a mandate for parameter A5. **EACH therefore suggests deleting parameter A5 and its two related indicators**.

Question 4: Do you agree with the list of parameters to describe the structure of incentives of a CCP's shareholders, management, clearing members and clients? If yes, are there additional parameters that should be added to the list? If not, please explain why and how you would suggest assessing the incentives in the methodology

EACH has a few observations to put forward regarding the list of parameters and **indicators** to describe the structure of incentives of a CCP's shareholders, management, clearing members and clients:

1. **Parameter B1 – "The CCP's ownership and capital structure"**
   Parameter B1 refers to the CCP's ownership and capital structure. This parameter is supposed to reflect the mandate under Article 9(15)(b) that refers to the '*structure of*

incentives of the shareholders, management and clearing members of CCPs and of the clients of those clearing members'. Contrary to the rest of the parameters in this section, we consider that this parameter B1 is **not aligned with the mandate in level 1** while the rest of the parameters under this section are. We therefore suggest:

i. **Deleting parameter B1 and its two related indicators**;
ii. Considering applying a **reduction in the SSITG** for those CCPs that deposit **customer funds at the Central Banks**.

2. **Parameter B2 – "To what extent the remuneration of the senior management is directly and contractually impacted following a default or non-default event"**
   a. **Indicator "*Average percentage of the CCP's senior management total variable remuneration subject to claw backs in the event of losses in excess of margins in a default and/or non-default events"***
      i. EACH wonders whether losses in excess of margins as included in this indicator could be due to non-default events and therefore suggests **deleting non-default events from this indicator**. In case there is a reason to keep non-default losses under this indicator, we would suggest **deleting the third indicator under parameter B2**[6] to avoid double-counting non-default losses.
   b. **Indicator "*Percentage of the senior management subject to variable remuneration claw back in case of non-default losses and/or production incidents (expressed as a % of senior management FTEs)"***
      i. As indicated above, in case ESMA sees a reason to keep non-default events in the first indicator of parameter B2, we would suggest **deleting this third indicator** under parameter B2 to avoid double-counting non-default losses.
      ii. In case non-default events are deleted from the first indicator under parameter B2, EACH would request **clarifications** in terms of what kind of production incidents should be taken into consideration and suggest that only 'material' production incidents are taken into account.

3. **Parameter B3 – "The clearing members' and clients' involvement in the CCP's risk governance"**
   a. **Indicator *"If clearing members are involved in the investment decision process, do they bear potential investment or custody losses?"***
      i. EACH suggests **providing the definition of "*involved in the investment decision process"***, for instance by specifying that clearing members could be considered involved in the investment decision process if they also have had a say in the investment decision policy of the CCP. The investment policy of the CCP is brought forward to the EMIR Risk Committee and subsequently put up for consultation to their clearing members (this may already happen if the investment policy is

[6] Percentage of the senior management subject to variable remuneration claw back in case of non-default losses and/or production incidents (expressed as a % of senior management FTEs)

part of the CCP rulebook). In any case, the investment policy of a CCP is also bound by the EMIR standards, which are quite strict.

b. **Indicator *"Are there incentives for clearing members and clients to participate in the default management process?"***
   i. EACH agrees with including an indicator concerning the incentives in place for clearing members and clients to participate in the default management process. Taking into account asset class specifics, in order to increase likelihood of a successful default management process, EACH considers it appropriate that CCPs have properly balanced incentives. These may include:
      - Juniorisation of the default fund – EACH Members generally agree that juniorisation seems to be one of the most effective incentives.
      - Mandatory participation in auctions or default management process steps
      - Fines
      - Rewards for those clearing members participating in auctions (e.g. seniorisation of the default fund)

c. **Indicator *"Among incentives, are there financial incentives or penalties to participate in auctions, or forced allocations rules where auctions fail?"***
   i. We consider that penalizing CCPs for not having in place measures such as penalties or forced allocation rules would interfere with the procedures following auctions agreed by CCPs and clearing members. **EACH therefore suggest deleting this indicator**.

Section 4.3 – Investment of the additional amount of pre-funded dedicated own resources

Question 5: Do you agree with the proposal that all EU CCPs may rely on alternative investments for the purpose of maintaining the SSITG?

Yes, EACH agrees with the approach adopted by ESMA that all CCPs may rely on alternative investments for the purpose of maintaining the SSITG, although we currently do not see an interest for CCPs to invest in asset classes other than the ones included in EMIR.

Question 6: Do you agree that this list of alternative investments shall be specified in the draft RTS?

Yes, EACH agrees that **the list of alternative investments shall be specified in the draft RTS.**

Question 7: Do you agree with the proposed list of additional investments for the purpose of maintaining the additional amount of pre-funded dedicated own resources under Article 9(14) of RRR? If not, please explain why? If yes, is there any type of asset that you would like to add to or remove from the list?

Yes, EACH agrees with the proposal by ESMA to allow CCPs to consider instruments already accepted as collateral from its clearing members, as described in the CCP's internal collateral policy, with the exception of bank guarantees, derivatives and equities.

In addition, we note that in paragraph 70 of the consultation ESMA considers the possibility of **extending the average time-to-maturity** of financial instruments to be considered as highly liquid **up to 5 years**. EACH is **very much in favour** of this proposal. An average time-to-maturity of **maximum 2 years is indeed too restrictive**, and in particular it raised issues during the COVID-19 emergency when the investment activity became much more challenging.

Question 8: Do you agree with the proposed procedure for triggering specified recovery measures where all or part of the CCP's pre-funded dedicated own resources allocated to cover SSITG are not readily available for CCPs? If not, please explain why?

Yes, EACH agrees with the proposed procedure for triggering specified recovery measures where all or part of the CCP's pre-funded dedicated own resources allocated to cover the SSITG are not readily available for CCPs.

Question 9: Do you agree with ESMA's proposed procedure for the compensation of non-defaulting clearing members? If not, please explain why?

EACH generally agrees with ESMA's proposed procedure for the compensation of non-defaulting clearing members. However, we would like to put forward the following comments:

- ECB rate for principal refinancing operations (5th bullet point of paragraph 81):
    - EACH would appreciate a clarification on whether this is the same as the **Main Refinancing Operations (MRO) rate**;
    - It is reported that "*the interest rate shall be the ECB rate for principal refinancing operations plus 2 percentage points*". We would like to request ESMA to clarify the **rationale behind adding the 2 percentage points on top of the ECB rate**.

Section 4.4 – Rules and practices of third country CCPs, and international developments

Question 10: Do you have access to different data and analysis that would contradict ESMA's conclusion that no further adjustment of the SSITG level based on competitiveness consideration is needed?

Regarding ESMA's analysis, and understanding the limitations related the availability and accuracy of data and conscious of the efforts made by the ESMA team to provide some metrics, EACH Members would like to make the following comments:

- **Metric 'CCP's own funds as a proportion of the total financial resources'** - While we understand that ESMA is trying to use some quantitative and objective data to compare EU CCPs with third-country ones, we believe that this comparison has unfortunately limited value given that, as opposed to the EU, the level of skin in the game in some of the international jurisdictions included such as the US is not set in law, and there is rather a mere requirement to have a skin in the game, without setting a minimum level. In addition, we consider that the data sample is limited (4 EU CCPs and 9 international CCPs, 4 of which belonging to the same group) and the data quality as included in the public quantitative disclosure is questionable.

  We would also like to stress our concerns regarding the comparison of the skin in the game with the resources provided by clearing members. The two have two very different outcomes: incentivising proper risk management in the case of the skin in the game and loss absorption in the case of resources provided by clearing members. We therefore consider that a comparison of both is not adequate. The resources provided by clearing may furthermore vary depending on the standards set in different legislations.
- **Metric 'SSITG impact on EU CCPs' capital position'** – EACH respectfully disagrees with the assumption made in the use of this metric that CCPs have capital buffers freely available and can therefore afford a SSITG. These capital buffers are usually there for different reasons (e.g. calculation of the CCP's economic capital to be used for example to deal with potential non-default events resulting in a higher amount than risk-based capital.

As an alternative to the two metrics above, EACH proposes the following objective metrics to analyse the competitiveness of EU CCPs:

- **Metric 1 - Do other jurisdictions have a requirement for a SSIG?**
  EACH understands that currently only Singapore has a rule for a SSIG. EACH suggest Authorities to take into consideration that an excessive amount of additional own resources would put them at severe disadvantage in the international landscape and damage their competitiveness, since the EU legislation is already one of the strictest and most robust worldwide for what concerns the capital requirements that CCPs are

subject to. For this reason, EACH recommends that the amount of SSIG should be as low as possible.

- **Metric 2 - Do other jurisdictions have in place a dedicated CCP recovery and resolution framework?**
  Similarly to what is mentioned in the comment under Metric 1 above, the EU has in place a dedicated and robust legislative framework for CCP recovery and resolution. EACH therefore recommends ESMA to also analyse whether third-country jurisdictions currently have a CCP recovery and resolution framework in place. We note the following:
  - US – CCPs designated as systemically important in the US: CME Inc and ICE Clear Credit. They could be resolved by the Federal Deposit Insurance Corporation (FDIC) under Title II (Orderly Liquidation Authority) of the Dodd-Frank Act (DFA) in order to ensure the continuity of critical clearing services. All other failing CCPs would be liquidated under Chapter 7 of the U.S. Bankruptcy Code.
  - UK – Dedicated CCP RR framework under public consultation phase.
  - Singapore – The Monetary Authority has a combined role as the prudential supervisor, resolution authority and lender of last resort. It currently imposes recovery and resolution planning on systemically important FMIs. This includes all approved CCPs.
  - Hong Kong – The Financial Institutions Resolution Ordinance which came into force in 2017, establishes a resolution regime for systemic financial institutions. It also covers the four Hong Kong CCPs, all of which form part of HKEX Group. The SFC is the supervisor and the resolution authority.
  - Canada – In 2017, the federal government proposed to introduce legislative amendments to the Payment Clearing and Settlement Act to implement the regime and allow the Bank of Canada to intervene if a systemically important FMI were to fail. The Bank of Canada has designated the Canadian Derivatives Clearing Service (CDCS) as systemically important.

In addition, according to Article 9(15)(d) of RRR, ESMA shall take into account "to preserve the competitiveness of internationally active Union CCPs, and the competitiveness of Union CCPs compared to third-country CCPs providing clearing services in the Union." While we understand the limitations related to the availability and accuracy of data and conscious of the efforts made by the ESMA team to provide some metrics, EACH Members would like to highlight that from our point of view the performed analysis is not complete compared to the mandate in Level 1. Specifically, while ESMA assesses "the competitiveness of Union CCPs compared to third-country CCPs providing clearing services in the Union", an assessment to "preserve the competitiveness of internationally active Union CCPs" is missing. **EACH therefore suggests that an assessment on the "competitiveness of internationally active Union CCPs" is added in the overall competitiveness consideration.**