
**EACH response to the ESMA consultation
on Draft RTS specifying the conditions for
recompense (Article 20(2) 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 specifying the conditions for recompense (Article 20(2) of CCPRRR)” (hereinafter called “The consultation”).

Section 5.2 – Order in which the recompense must be paid

Question 4: Do you agree with the proposed definition of profit for the purpose of the recompense scheme?

Yes, EACH agrees that “profits” shall have the same meaning as defined in the applicable accounting framework in the CCP’s jurisdiction.

Section 5.3 – Maximum number of years and maximum share of the CCP’s profits

Question 5: Do you agree with the proposed values for the maximum share of profits and maximum number of years for the recompense to be paid? If not, please explain why.

As a first comment, we would like to underline that, in principle, EACH opposes any types of compensation other than those included in the Level 1, i.e. the compensation scheme under Article 20 and the one under Article 27.6. The latter states that the resolution authority may require the CCP to compensate non-defaulting clearing members for their losses stemming from the application of loss allocation tools, where the losses are in excess of those that they would have borne under the CCP’s rulebook, provided that the non-defaulting clearing member would have been entitled to claims under the No Creditor Worse Off (NCWO) principle. We agree that any compensation scheme decoupled from the limitations posed by the NCWO principle would be detrimental for the incentives structure on which a CCP is based, as clearing members may be incentivized not to efficiently cooperate with the CCP in the default management process or the recovery phase in order to reach as quickly as possible the compensation stage.

We would like to underline that an excessively high portion of CCP profits dedicated to compensating non-defaulting clearing members as per Article 20 would most likely endanger the commercial viability and attractiveness of the CCP. This could, in the long term, potentially

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affect financial stability. We therefore agree with ESMA that compensation should be limited both in terms of number of years and in terms of maximum amount of profits to be shared with the non-defaulting clearing members. We also understand the intention to limit the application of compensation to the use of a specific tool to cover non-default losses, but would like to underline that said compensation should **only be applicable in case the CCP deviates from the rulebook agreed with its clearing members.**

EACH however **disagrees** with ESMA's proposal of dedicating a maximum share of profits of 70% for up to 10 years to recompense clearing members. We detail our rationale in the following answers.

Question 6: If you prefer a different set of numbers for the maximum share of profits or maximum number of years, please explain why you prefer those levels.

As indicated in our response to Question 5, we respectfully disagree with the proposal of dedicating a maximum share of profits of 70% for up to 10 years to recompense clearing members, given that we consider that it does not adequately balance the distribution of a fair share of profits to clearing members with the long-term viability of the CCP. As an alternative we would like to suggest an **approach that is very close to Policy Option 3** as defined in the table at page 22 of the consultation¹.

More specifically, **we suggest a compensation scheme that foresees dedicating to clearing members a share of profits between 10% and 25% for up to 5 years.** According to the CCPs, this would ensure that clearing members receive a fair share of CCP profits, but at the same time protects the CCP from becoming less attractive to other investors and potential shareholders.

We notice that page 14 of the consultation ESMA includes a table (Table 1) reporting the amount of retained earnings as a share of the CCP's profits, for the years 2017, 2018 and 2019, for 7 EACH Members. Looking at the amount of retained earnings, ESMA concludes that *"setting the maximum share of profits at 70% would be appropriate, as it would allow the competent authority sufficient flexibility to adapt the share of profits to the specific situation of the CCP whilst ensuring that the CCP have the possibility to manage part of its annual profits as it sees suitable"*. Commending ESMA's efforts to provide a quantitative justification to its proposals. EACH has extended the analysis to 10 EMIR-authorized CCP (see Table 1 below), excluding those two that have a full profit and loss transfer agreement with their parent company. We notice that, for the three years considered, **6 CCPs retained 100% of their earnings**, while other **3 have retained in 2019 over 35% of their earnings**. It is important to specify that such retained earnings can be used for various purposes, e.g. strengthen their capital base or, from a recovery and resolution perspective, they can be used for instance to address non-default losses carried by the CCP itself, or provide for a loss-buffer during the end of recovery/resolution phase.

¹ To set the maximum number of years to a very short period, e.g. **3 years** and to determine the maximum share of the CCP's annual profits that could be used for the recompense payments also very low, e.g. **20-30%**. leaving a fairly wide scope for distribution of profits

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We therefore do not see the rationale behind the conclusion that a share of profits of 70% would be suitable, but rather support an approach that foresees dedicating to clearing members a share of profits between 10% and 25% during a period of up to 5 years.

Table 1: Retained earnings as a share of the CCP's profits

CCP	2019 (%)	2018 (%)	2017 (%)
CCP 1	100	100	100
CCP 2	10	14	10
CCP 3	38	5	5
CCP 4	38	42	N/A
CCP 5	100	100	100
CCP 6	36	0	8
CCP 7	100	100	100
CCP 8	100	100	100
CCP 9	100	100	100
CCP 10	100	100	100