29 juillet 2011

CPSS-IOSCO : CONSULTATIVE REPORT ON PRINCIPLES FOR FINANCIAL MARKET INFRASTRUCTURES
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FBF, AFTI AND AMAFI'S RESPONSE

The French Banking Federation ("FBF") represents the interests of the banking industry in France. Its membership is composed of all credit institutions authorised as banks and doing business in France, i.e. more than 500 commercial, cooperative and mutual banks. FBF member banks have more than 25,500 permanent branches in France. They employ 500,000 people in France and around the world, and service 48 million customers.

The Association Française des Professionnels des Titres ("AFTI") is the leading association in France and within the European Union representing the post-trade industry. The AFTI has over more than 100 members, all actors in the securities market and back office businesses: banks, investment firms, market infrastructure, issuers.

The Association Française des Marchés Financiers ("AMAFI") has more than 120 members representing over 10,000 professionals who operate in the cash and derivatives markets for equities, fixed-income products and commodities. Nearly one-third of members are subsidiaries or branches of non-French institutions.

Together **"The Associations"**.

PART I - GENERAL COMMENTS

The Associations welcome the opportunity to respond to the "*Consultative report on principles for financial market infrastructures*" since their members are very much involved in this activity.

As general remarks, we would like to underline our agreement on most of the principles developed by CPSS-IOSCO in this consultative report.

We welcome in particular the conceptual clarity in which the Financial Market Infrastructures are framed throughout the Report insuring a level playing field and applying these principles to FMIs irrespective of their owners (private or public sector) Also, market infrastructures are prevented from leveraging their central position by unfair competition with their participants, in the context of their expansion into non-infrastructure services.

Inter alia, the Consultative Report recognises in several occasions the following facts:

- Market Infrastructures are CENTRAL to the market; hence:
- Their rules and procedures are common to all participants and they are public; therefore these rules exclude bilateral relationships between financial institutions and their customers (p. 7);
- Without appropriate regulation, Market Infrastructures have in theory the power to leverage their central position against their participants;
- The immediate commercial interest of Market Infrastructures can lower their standards of risk management and thus potentially impact the whole market.

Therefore FMIs have to be stringently regulated and supervised; they should not be transformed into regulators themselves. A positive evolution integrated in the Consultative Report is that regulation on FMIs is necessary: it is clearly stated that market forces, alone, cannot do the job.

Considering the FMI conflicts listed supra, we strongly oppose conferring regulatory and enlarged supervisory functions to FMIs which would go beyond their direct participants. This trend appears clearly especially in Principle 19 ("Tiered participation arrangements"), and as well in Principle 1 ("Legal basis"). Principle 19 confers upon the FMI regulatory powers on all market participants, while Principle 1 seems to create a new "rule book" for the whole market where the rules of the FMIs are bundled together (and put on the same level) with laws and regulations promulgated by the regulators[1].

FMIs can legitimately rule their relationship with their direct participants, provided that these rules would be uniform, public (transparent) and approved by the regulator/supervisor. But the negative externalities, in terms both of systemic risk and fair competition, of giving regulatory powers to the FMIs on the whole market, by far exceed the potential advantages.

[1] In respect, in paragraph 3.1.4 of this Principle 1, using the verb « *interpret* » in the sentence « *A legal opinion or analysis, among other things, should identify and, where necessary,* ***interpret*** *the laws and regulations applicable to an FMI's operations and services*" is misleading.

Additionally, the Associations want to underline that any rule upon commercial banks should be clearly separated from the Principles. The Consultative Report states that, despite not having been reviewed nor included in the Principles for FMIs, the “Marketwide Recommendations” of the former set of standards “remain in effect” (p. 6, paragraph 1.7). Indeed, the marketwide recommendations are not included in the Principles on Market Infrastructures; they are now listed in a separate annex. It should be then clarified to whom those “Marketwide Recommendations” will be applicable.

This statement is counterproductive, since these “Marketwide Recommendations” (“trade confirmation”, “settlement cycle”, “securities lending”, “protection of customers securities” etc) were partly responsible for the uncertainty regarding the scope of application which was inappropriately extending beyond the market infrastructures. We would welcome a separate and comprehensive work of CPSS and IOSCO regarding the regulation of participants to market infrastructures with a clear delimitation between infrastructure regulation and market participants’ activity.

The Associations also support the aim of limiting systemic risk since the financial crisis shows the paramount importance of these kinds of infrastructures to prevent such risk. On this aspect, one cannot lose sight of the fact that these Principle are “minimum standards”, and that their goal is not to undermine efficient regulation where it already exists. In particular, for instance, while the Principles recommend to reduce to a maximum extent the credit risk taken by CSDs, especially by adopting DVP (“exchange of value settlement”) and by carrying out the money settlement in central bank money, the fact that the Principles provide remedies to the situations where commercial bank money is used does not imply that future regulations based on the Principles should feel deemed to propagate this lesser desirable arrangement when a better one is already in practice.

In this regard, having to encompass the differences in systems worldwide, the definition of CSDs is still disappointing. The primary role of CSDs is indeed not to hold (or to maintain) securities accounts (as would do a banking intermediary) but to be the main entity in charge of ensuring the integrity of an issue by ensuring the reconciliation between on one side the issued securities deposited in the issuer’s account (either at registrar or at the CSD level) and on the other side the securities in circulation. The CSD is indeed the keystone of the integrity of the issuance of securities (even when this function is exercised taking into account the existence of registrars).

In discharging these functions CSDs play a specific and central role that guarantees the safety, soundness and efficiency of the securities market. This specificity is recognized across Europe and abroad and enshrined in dedicated national regulations. In this respect, the CSD should be a “risk-free environment”. This means that the CSD should not be allowed to take any other forms of risk than the ones inherent to its activity, i.e. operational risk. Moreover, the entity that fulfils these functions, should not, ipso facto, be authorised to fulfil any other functions (currently referred to as “ancillary functions”) such as banking functions which can entail considerable credit exposure.

The Associations are of the opinion that all other services but CSD services should be provided for on a strictly segregated basis. This should apply to all commercial services, such as credit functions or issuers’ services that should be provided under a different license, by different entities as the CSD functions should, in no circumstances, be subject to any adverse consequence arising from commercial services activities. As a consequence, should a company operating a CSD be willing to engage into non CSD services, it should be subject to a mandatory “2+2” model ,whereby different licenses should be applied for by different entities so that CSD functions are performed by a regulated entity that is not engaged in other activities.

The remedies suggested in the Report to alleviate credit risk in cases where commercial bank money is used, are disappointing as well. The central and systemic role of CSDs is reinforced by the fact that, most of the time (as underlined by the report), a CSD operates a central settlement platform (SSS). This makes the exposure of a CSD to credit risk especially undesirable: systemic risk is enormous in case of settlement in the books of the CSD. Unfortunately, the Report does not address the necessary ring-fencing of the infrastructure from these risks by any specific disposition and stringency in its recommendations appears lacking.

The Principles cannot justify to export / import less stringent rules and practices in countries which already benefit from higher risk management standards. In this regard, we welcome very much the axis developed for the international cooperation between market authorities and central banks. In particular, the necessity, for market authorities, to justify to their peers their oversight and regulatory choices while applying the standards is a positive evolution.

Thus we hope that the application of the Principles will drive towards an upgrade of the global and individual safety of Market Infrastructures, and will not translate into a race to the bottom taking into account that some recommendations will appear less stringent in some markets than the existing organisation in place.

This issue is of particular relevance in the context of the Markets infrastructures' interoperability: it remains indeed unclear if the compliance of linked infrastructures with the relevant dispositions disseminated throughout the Principles can be considered as sufficient to force national authorities to authorise such links.

Concerning the payments business domain (e.g. Large Value Payments), the Associations support the comments made by the Target Working Group from the European Banking Association even if these comments are not systematically repeated here after.

Specifically for CCPs, we would like to stress several points:

The first one touches on the extend to which a surviving member could be involved in case of a participant's default. It seems to be generally admitted that the "loss-sharing" is a kind of "natural component" of a CCP set-up. We understand the idea of "mutualisation" to keep a CCP going on but don't believe it could still apply: firstly, CCPs are now commercial companies and some may be tempted to use their risk management policy as a commercial argument to gain new clients. As a participant, a clearing member has no idea of the level of business risk a CCP has decided to face. Secondly, CCPs are no more dedicated to a single market and / or they no longer act on a stand alone basis in case of interoperability agreements; as a consequence it could be more difficult for a clearing member's community to agree on absorbing collectively the losses in order to save "their" CCP, especially to cover the default of a participant (or a linked CCP) on a market or market segment they are not aware of, even if there is a sound legal basis as said in 3.4.15. From our point of view, the default waterfall should be stricter than what is currently proposed and the "loss-sharing" should not be considered as something normal. In this regard, we support a waterfall procedure as proposed in the future European Market Infrastructure Regulation where margins posted by non-defaulting clearing members shall not be used by a CCP to cover losses resulting from the default of another clearing member.

We also want to highlight that the safekeeping of the assets (cash or securities) posted by a participant should be fully secured. As far as the CCP owns direct accounts either in a National Central Bank or a CSD, we consider that these assets are safe. But in case where a CCP entrusts a commercial bank with the safekeeping of the assets, we are much more dubious regarding the related level of safety. Obviously the amounts are high due to the destination of the deposits (collateral/margin). But in case the bank defaults, participants will

get their assets back if they are segregated and, as far as cash deposits are concerned, up to the legal threshold if any.

Finally, regarding Principle 14 "Segregation and portability", we would like to underline that segregating proprietary positions from clients' positions when calculating the margin requirements is logical and should be strongly promoted, going beyond this (i.e. segregation per individual client) needs further analysis. The first question to be asked should be "Who is the customer?" Participants of a CCP are Clearing Member Firms ("CMF"). They have commercial relationship with Trading Member Firms ("TMF"). Clearly the customers of a CMF are the TMF whereas Order Givers are the customers of the TMF. Indeed the issue is: what is the objective of CPSS IOSCO when introducing the notion of customers/indirect participants? Which are the entities targeted? Who should be protected?

PART II – SPECIFIC RESPONSES FOR CPSS-IOSCO COVER NOTE QUESTIONS

Principle 4: Credit risk

An FMI or its participants may face credit risk in the FMI's payment, clearing and settlement processes. Credit risk is the risk that a counterparty will be unable to meet fully its financial obligations when due or at any time in the future.

The credit risk principle requires a payment system that is systemically important, a CSD or an SSS to cover its *current credit exposures* and, where they exist, *potential future credit exposures* to *each* participant fully with a high degree of confidence using collateral and other equivalent financial resources. It also requires a CCP to cover its *current credit exposures* and its *potential future credit exposures* to *each* participant fully with a high degree of confidence using margin and other financial resources. A CCP is also required to maintain *additional* financial resources sufficient to cover a wide range of potential stress scenarios identified in regular and rigorous stress testing.

With respect to the particular stress scenarios for which CCPs should hold additional financial resources, the CPSS and IOSCO are considering, and requesting comment on, the establishment of a minimum credit requirement that (1) all CCPs should include the default of the one participant and its affiliates that, in the aggregate, would potentially cause the largest credit exposure in extreme but plausible market conditions (that is, a "cover one" minimum requirement); (2) all CCPs should include in their stress scenarios the default of the two participants and their affiliates that, in the aggregate, would potentially cause the largest credit exposure in extreme but plausible market conditions (that is, a "cover two" minimum requirement); or (3) a CCP should be subject to either the "cover one" or the "cover two" minimum requirement, depending on the particular risk and other characteristics of the products it clears, the markets it serves and the number and type of participants it has. More specifically, the CPSS and IOSCO would welcome comments on the following questions:

- **<u>Question 1:</u> What are the pros and cons of establishing for credit risk (1) a "cover one" minimum requirement for all CCPs; (2) a "cover two" minimum requirement for all CCPs; and (3) either a "cover one" or a "cover two" minimum requirement for a particular CCP, depending upon on the risk and other characteristics of the particular products it clears, the markets it serves and the number and type of participants it has? What potential risk, competitiveness or other concerns might arise if certain CCPs that clear certain products would be subject to a "cover one" minimum requirement, while certain other CCPs that clear certain other products would be subject to a "cover two" minimum requirement? How and to what extent could these concerns be addressed?**

- **<u>Question 2:</u> Which risk and other characteristics of the products cleared by a CCP are relevant in weighing the pros and cons of a "cover one" versus a "cover two" minimum credit requirement for a CCP? In particular, to what extent are any or all of the following product and market characteristics relevant: OTC versus exchange-traded; mandatory versus voluntary clearing; "cash" versus "derivative"; the duration, volatility and degree of leverage; the number and type of CCP participants; the degree of market concentration; and the availability and reliability of prices from continuous, transparent and liquid markets?**

The Associations believe credit risk principles should be as consistent as possible with those currently established in the European Market Infrastructure Regulation (EMIR) or the Dodd Frank act, with the aim to insure a level playing field since such rules could have important prudential impacts.

In this way, and from a European point of view, we support a "cover two" principle only for CCPs since such principle is expected to be consistent with the future EMIR regulation. I EMIR is based on the current practice of CCPs.

On the contrary, we do not support the third option permitting to choose between a "cover one" or a "cover two" "*depending on the particular risk and other characteristics of the product [the FMI] clears, the markets it serves and the number and type of participant it has".* Even if such a possibility seems attractive as it offers a kind of flexibility with regard to the particular characteristics described above, in practice it could hamper efficient implementation as clear definitions would be needed regarding of products, types of participants subject to a "cover one" or a "cover two" principle, etc. Finally, a mandatory "cover two" principle will favour a level playing field between FMIs.

However, FMIs which are not CCPs, should, according to the Associations, be subject to a "cover one" requirement.

We would like to add the following two comments:

Firstly, and most importantly, we want to strongly underline that for a CCP, stringent membership criteria, and hence the financial strength of its clearing members, are crucial for a sound risk management, when deciding on access and when monitoring of members on an ongoing basis. These financially sound clearing members then manage their own credit risk on their clients of lesser creditworthiness, which would be ring-fenced from the CCP as indirect participants. While mandatory clearing is progressively enforced globally and will give rise to a progressive extension of the material scope covered, it is of utmost importance that the quality of membership in CCPs is preserved, despite the commercial interest of the CCPs themselves.

Second, while we support the introduction of specific minimum requirements, it is important that such minimum requirements avoid the suggestion that a simple quantitative standard is a substitute for prudent risk management.

We consider that it is far more important that a FMI's credit requirement is based on an assessment of the relevant risk factors such as the quality of the counterparties to a given FMI and the products serviced by the FMI. The importance of each criterion would vary depending upon the FMI.

Additionally, given the Basel Committee's proposal that "qualifying CCP" status depends on compliance with these CPSS-IOSCO principles, there is a risk that the breach of a known number standard (either "cover one" or "cover two") could result in a sudden change in capital requirements. Such a sudden change gives rise to serious concerns about the settings among market participants and CCPs, and the potential disruption caused by the fact that the CCP is in breach.

Principle 7: liquidity risk

The liquidity risk principle requires an FMI to maintain sufficient liquid resources to effect same-day and, where appropriate, intraday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios.

With respect to the particular stress scenarios for which a payment system that is systemically important, a CSD or an SSS should hold sufficient liquid resources, the CPSS and IOSCO are considering and seeking comment on the establishment of a minimum liquidity requirement that (1) all such FMIs should include in their stress scenarios the inability of the one participant and its affiliates with the largest aggregate payment obligation to settle that obligation (that is, a "cover one" minimum requirement); (2) all such FMIs should include in their stress scenarios the inability of the two participants and their affiliates with the largest aggregate payment obligations to settle those obligations (that is, a "cover two" minimum requirement); or (3) such an FMI should be subject to either the "cover one" or the "cover two" minimum requirement, depending on the particular risk and other characteristics of the payment obligations it settles.

With respect to the particular stress scenarios for which a CCP should hold sufficient liquid resources, the CPSS and IOSCO are considering and seeking comment on the establishment of a minimum liquidity requirement that (1) all CCPs should have sufficient liquid resources to meet the required margin payments and to effect the same-day close out or hedging of the one participant and its affiliates with the largest potential open positions in extreme but plausible market conditions (that is, a "cover one" minimum requirement); (2) all CCPs should have sufficient liquid resources to meet the required margin payments and to effect the same-day close out or hedging of the two participants and their affiliates with the largest potential open positions in extreme but plausible market conditions (that is, a "cover two" minimum requirement); or (3) a CCP should be subject to either the "cover one" or the "cover two" minimum requirement, depending on the particular risk and other characteristics of the products that it clears, the markets it serves and the number and type of participants it has.

With respect to the establishment of a minimum liquidity requirement, the CPSS and IOSCO would welcome comments on the following questions:

- **<u>Question 3:</u> What are the pros and cons of establishing for liquidity risk (1) a "cover one" minimum requirement for all FMIs; (2) a "cover two" minimum requirement for all FMIs; and (3) either a "cover one" or a "cover two" minimum requirement for a particular FMI, depending on the risk and other characteristics of the particular payment obligations it settles, the products it clears, the markets it serves and the number and type of participants it has? What potential risk, competitiveness or other concerns might arise if certain FMIs that settle certain payment obligations or that clear certain products would be subject to a "cover one" minimum requirement, while certain other FMIs that settle certain other payment obligations or that clear certain other products would be subject to a "cover two" minimum requirement? How and to what extent could these concerns be addressed?**

- **<u>Question 4:</u> Which risk and other characteristics of the payment obligations settled by a payment system, CSD or SSS are relevant in weighing the pros and cons of a "cover one" versus a "cover two" minimum liquidity requirement for such an FMI? Which risk and other characteristics of the products cleared by a CCP are relevant in weighing the pros and cons of a "cover one" versus a "cover two" minimum liquidity requirement for a CCP? In particular, to what extent are any or all of the following risk and other characteristics of the payment obligations settled or the products cleared by an FMI relevant: OTC versus**

exchange-traded; mandatory versus voluntary clearing; "cash" versus "derivative"; the duration, volatility and degree of leverage; the number and type of CCP participants; the degree of market concentration; and the availability and reliability of prices from continuous, transparent and liquid markets?

First of all, the Associations welcome developments on liquidity risks of CCPs.

In their response on the 2010's consultative report on "*Recommendation for Central Counterparties to OTC Derivatives CCPs"*, the Associations already underlined their belief that a CCP should always be in a position to rapidly and securely obtain the necessary liquidity, provided by the central bank, to limit systemic risk.

In the event of a major financial crisis, central banks have a major role to play in order to solve the crisis. In case of a default of one of its participants, the CCP needs to be able to access liquidity provided by a central bank as rapidly as possible (on an intraday or overnight basis).

In this context, the CCP must have a direct link with the central bank, which seems to be difficult if it is not under its supervision.

This is the reason why the Associations have always supported the necessity for a FMI, as far as possible, to have a banking status with an agreement limited to its activity.

Besides, we understand from this principle and its key considerations that it has currently not been decided whether such liquidity risk framework should be made on the hypothesis of the default of one or two participants. Concerning the future European regulation on market infrastructure, such hypothesis is currently based on the default of two clearing members for CCPs.

In the case of payment systems, the prime requirement should be that the FMI ensures that only high quality and liquid collateral with appropriate haircuts is used. **On this basis we suggest that settlement risk in payment systems is treated as liquidity risk and not as credit risk.**

Liquidity risk will remain with the participants either directly or through some form of common collateral or liquidity pool. The payment systems responsible for implementing rules and procedures to make sure that adequate liquidity / collateral is available for settlement.

Subject to the conditions listed below, "cover one" should be the minimum requirement for payment systems. A major reason for this is the likely limit on the availability of suitable collateral which may also be required for a range of other purposes including Basel regulatory requirements, monetary policy operations and other FMIs. Our concern is that stipulating a minimum "cover two" requirement could result in some institutions relying on other participants' liquidity by delaying outward payments which would not only reduce operational efficiency but also potentially create additional risk for the other participants who may effectively be acting as unsecured liquidity providers.

However, this proposal is subject to the following conditions.

- Group situations where participants are financially linked are treated as one participant for this purpose and the phrase “participant and its affiliates” is not considered sufficiently explicit. Instead, it should be replaced with more formal group criteria, possibly based on Basel principles. It follows that several participants (and their affiliates) may be counted as a single entity for “cover one” purposes.

- When applying this requirement, it must be possible for payment systems to measure and control the highest intra-day credit risk, where applicable, and this requirement should be applied to such risk. For DNS systems, the term “intra-day” should be construed as being the highest credit risk arising during the deferred settlement process based on the underlying legal infrastructure. It is acknowledged that some payment systems may require time to accommodate this requirement but it is considered important that the underlying principle should be established.

- Robust default procedures , including where two or more participants fail simultaneously, with mandatory testing at least annually and more frequently if material changes are made, should be put in place so that in a crisis situation they can be implemented without delay.

As mentioned above, consistency should be reached with both EU and US regulation.

Principle 14: segregation and portability

Principle 14 on segregation and portability is only applicable to CCPs. The substantially new principle recommends that CCPs should have segregation and portability arrangements that protect customer positions and collateral, to the extent practicable and where feasible and supported by the legal framework. This qualifying language recognises that there may be market structure or legal impediments to a CCP facilitating segregation and portability in the cash markets.

The principle is designed to offer CCPs flexibility in achieving segregation of customer collateral and identifies the advantages and disadvantages associated with the use of omnibus and individual accounts. The principle also provides expanded guidance on the way that margin is collected (gross or net basis) by the CCP and explains how different levels of customer protection can be achieved. While the principle presents options, the overall objective is to protect customer positions and collateral, particularly in the case of insolvency of a participant.

The CPSS and IOSCO request comment on challenges associated with establishing segregation and portability regimes for CCPs. In particular, while no specific model of segregation and portability is prescribed in the relevant principle, the CPSS and IOSCO would particularly welcome comments on the following questions:

- **Question 5:** What are the different models and approaches to establishing segregation and portability? What are their pros and cons respectively, for example in terms of efficiency and level of protection that can be achieved?
- **Question 6:** In view of the different options and models that may exist, is there any one option or model in particular that could usefully serve as a minimum requirement? Would it is be possible to identify a specific approach to segregation and portability that could be defined as best practice?
- **Question 7:** Would it be helpful to distinguish between different types of customers, such as by the degree of tiering or by domestic or cross-border activity? Please explain.
- **Question 8:** Would it be helpful to distinguish between different types of products? If so, please explain why and how.
- **Question 9:** What are the existing legal constraints that limit segregation and portability?

It is the Associations opinion that segregation and portability arrangements are of utmost importance for the protection of customers and their positions in case of a participant's default.

We then support the key considerations developed in this Principle 14, knowing that this principle is dedicated to CCPs.

However, as far as we understand the various types of possible segregation arrangements, the US (through the Dodd Frank Act) and the EU (through EMIR) legislations currently discussed, will impose their own conception of the level of segregation, and the consequences attached (including prudential consequences). In its December 2010

consultative document on "*Capitalisation of bank exposures to central counterparties*" the Basel Committee proposes a favourable treatment for 'bankruptcy-remote' collateral for clearing members as well as the favourable risk weight of qualifying CCPs for non-member banks exposures provided that their assets are segregated and bankruptcy-remote from the clearing members'. We would like to draw the Committee's attention to the fact that the concept of bankruptcy-remote collateral is not aligned with the CCPs' various segregation models prevailing today and relies too much on national bankruptcy laws which are far from being aligned. In addition, our understanding is that the concept of "bankruptcy remote" is only relevant for securities, cash being commingled. Therefore, the Associations suggested in their response to the consultative document to adapt the most favourable treatment on a notion of "*appropriate segregation*" as the current legislation both in the EU and in the US are about to precisely define the level of segregation expected from CCPs.

Furthermore, this Principle should provide a clear definition of "customers" since many types of customers exist. Is it the TMF? The client of the TMF? Indeed most often it is up to the CMF (the CCP's participant) to post collateral and to require collateral from its customers. Acting solely as a TMF, the GCM's customer could then in turn ask its own customers to provide collateral to cover their open positions. Then, in the books of the TMF as well as in those of the GCM or of the CCP there are accounts reflecting the amount and the ownership of each deposit. The aim of Principle 14 is to protect the positions/collateral of a customer of a participant by using "an account structure that enables it …/… to identify and segregate positions and collateral belonging to customers of a participant". That said, who should be the owner of the account in the CCP's books? The customer of the participant or the collateral provider or the beneficiary of the collateral?

Re-hypothecation of non-cash collateral provided to an FMI should be prohibited as it would create additional types of risk, thus limiting the purpose of collateral as a means to reduce counterparty and market risks.

It is our opinion that securities collateral should be segregated and cash collateral should be held with the relevant central bank.

Finally, this Principle 14 should apply to all asset classes.

Principle 15: general business risk

In addition to the credit, liquidity, and other related risks that may result from the default of participants, an FMI also faces general business risk. The inability of an FMI to continue as a going concern could pose systemic risk to its participants and the broader financial market. The new general business risk principle would require an FMI to identify, monitor and manage its general business risk and hold sufficiently liquid net assets funded by equity to cover potential general business losses so that it can continue providing services as a going concern. This amount should at all times be sufficient to ensure an orderly wind-down or reorganisation of the FMI's critical operations and services over an appropriate time period.
The CPSS and IOSCO are considering, and requesting comment on, the establishment of a specific minimum quantitative requirement for liquid net assets funded by equity. More specifically, the CPSS and IOSCO request comment on the following questions:

- **Question 10: What are the pros and cons of establishing a quantitative and/or a qualitative requirement for the amount of liquid net assets funded by equity that an FMI should hold to cover general business risk?**

- **Question 11: If a quantitative requirement is established, what are the pros and cons of setting this amount equal to six, nine or twelve months of operating expenses?**

Regarding question 10, the Associations remind that minimum amount proposed by EMIR for a CCP is 10 millions Euros.

Regarding operating expenses (question 11), quantitative requirements should be equal to 6 months of operating expenses. However, such a provision is not relevant for payment systems.

Principles 18 to 20: access and interoperability

The CPSS and IOSCO consider that mandatory clearing and the integration of international financial markets will increase the importance of ensuring fair and open access to FMIs and, relatedly, of links between FMIs in general and CCPs in particular. The evolution of global clearing structures may affect the degree of tiering, the number of CCPs in operation and interoperability arrangements that may exist or be established between CCPs and other FMIs. The CPSS and IOSCO would welcome comments on the future evolution of global clearing structures and the role that interoperability may have in this regard.

More specifically, Principle 18 emphasises that an FMI should establish fair and open access to its services, for both direct and indirect participants, with any restrictions justifiable only in terms of specific issues impacting the safety and efficiency of the FMI or the markets it serves.

Principle 20 addresses link arrangements between FMIs and establishes new standards for CSD-CSD and CCP-CCP links and special considerations for links established by a trade repository. A link is a contractual and operational arrangement between two or more FMIs that connects the FMIs directly or indirectly. This new principle reflects the growing importance of link arrangements in the financial markets also as a result of mandatory clearing and the importance of establishing strong standards to ensure that FMIs have a well-founded legal basis that supports the design and operation of the link. The principle recognises that the type and degree of risk will vary according to the design and complexity of the linked arrangement and provides

guidance as to how each FMI should identify, monitor and manage all link-related risks. The CPSS and IOSCO acknowledge that links are an important source of additional operational and financial risks, which call for more stringent requirements. Against this background, the CPSS and IOSCO specifically request comment on challenges associated with establishing links between FMIs.

Regarding interoperability arrangements, we understand that CPSS-IOSCO considers interoperability between CCPs.

As already mentioned, the Associations do not support interoperability arrangements for the following reasons:

- First of all, implementation of interoperability is difficult, as evidenced by the fact that, in the European area, after about 4 years of work done by the banking and financial industry and monitoring of the Code of Conduct by the European Commission, interoperability links have not yet been implemented, despite multiple demands. Since the market infrastructures have published access and interoperability guidelines, more than 80 demands have been issued but none has as yet been put in place.

  This can be due to, amongst others, the following reasons:

  - The complexity of building interoperability links between CCPs due to obstacles that prevent competition on an equal footing ;

  - Players have realized that answering to all requests for access and interoperability would result in a kind of spaghetti network.

- Secondly, the development of interoperability could lead to a propagation of systemic risk between interconnected CCPs, which is the opposite result of what is envisaged by the clearing of OTC derivatives via CCPs.

To conclude, even if it seems difficult to avoid interoperability arrangements, they should be strictly controlled.

Principle 19 addresses the risk linked to tiered participations. We believe that it would be difficult for an FMI to identify, understand and manage the risks arising from indirect participants and that it may force FMIs to take on an inappropriate role.

For CCPs, for example, we need once again to determine who the client is. The one who executes the order on a market (*i.e.* TMF[2])? The one who wants to buy/sell? Even if the CCP is authorised to get information about the "client", how would this information be used? How would the CCP determine if there is a risk on this client or not? And what could it do then? Ask the participant to stop working with its client? Increase the margin requirements?

The same difficulties may occur for CSDs. How could they get information on customers from participants where they could be their competitors in providing custody service?

[2] Trading Member Firm

More broadly, we believe that the requirements within this principle 19 are excessive and unnecessary. It is the role of direct participants to manage the risks of their indirect participants. The CPSS-IOSCO proposals involve a FMI in monitoring and assessing “indirect participants”, which includes end-users. While this expansion of oversight may provide benefits, many FMIs do not currently have the systems or infrastructure to monitor or assess indirect participant risk. Accordingly, without further requirements from policy-makers at the local level, these proposed standards may not lead to practical risk management improvements.

Client risk is the risk of the clearing member or CSD participant. Participants are responsible for managing this, not the FMI, and we do not believe the FMI can or should be given this responsibility. Furthermore, the FMI is not privy to the necessary degree of detailed information about its GCMs’ clients, and we do not believe it is either feasible or necessary to make them aware. The negative externalities, in term both of systemic risk and fair competition, of giving powers to the FMIs on the whole market, by far exceed the potential advantages.

For these reasons, this Principle 19 should be deleted.

About Principle 18 and access requirements we want to recall that they need to be objective, non-discriminatory and publicly disclosed to provide open participation to market participants, market infrastructures, trading venues and service providers and they should only be restricted where this would pose a risk to the efficient and safe functioning of an FMI.

Any links regarding post-trade infrastructures and other third-party service providers will need to be closely monitored to mitigate any operational and legal risk.

Finally, communication systems and procedures should be secure to enable efficient interconnectivity.

Regarding the links between CSDs, there should be only one system providing settlement finality for any transaction (cf. comment of Principle 8) and it seems that this issue is not addressed in the Report. The circulation of conditional finality throughout linked systems propagates systemic risk, by submitting all participants of several domestic markets to unexpected unwinding of settlement with systemic domino effects.

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The Associations would like to point out the following comments on Principles developed in this consultative report.

PART III – OTHER COMMENTS ON MARKET INFRASTRUCTURE PRINCIPLES

General organisation

Principle 1: Legal basis

An FMI should have a well-founded, clear, transparent, and enforceable legal basis for each aspect of its activities in all relevant jurisdictions.

Key considerations

1. The legal basis should provide a high degree of certainty for each aspect of an FMI's activities in all relevant jurisdictions.
2. An FMI should have rules, procedures, and contracts that are clear, understandable, and consistent with relevant laws and regulations.
3. An FMI should be able to articulate the legal basis for its activities to relevant authorities, participants, and, where relevant, participants' customers, in a clear and understandable way.
4. An FMI should have rules, procedures, and contracts that are enforceable in all relevant jurisdictions, even when a participant defaults or becomes insolvent. There should be a high degree of certainty that actions taken under such rules and procedures will not be stayed, voided, or reversed.
5. An FMI conducting business in multiple jurisdictions should identify and mitigate the risks arising from any potential conflicts of laws across jurisdictions.

The Associations support the key considerations mentioned above.

Regarding the laws and regulation governing the rights and interests in financial instruments, settlement finality and netting, the Associations are of the opinion that the applicable law should be defined with respect to the localisation of the account where the relevant financial instruments are registered. In the European legal framework, this principle is enshrined in the Settlement Finality and the Financial Collateral directives.

We have major concerns with the way the Principle 1 is considered in the report. For instance as it appears in the following excerpts:

- "*The legal basis defines, or provides the foundation for relevant parties to define, the rights and obligations of the FMI, its participants, and, where relevant, participants' customers.*" (p.19, par 3.1.1)

- "*The legal basis consists of the legal framework and the FMI's rules, procedures, and contracts*" (p.19, par 3.1.2).

- "*One recommended approach to articulating the legal basis for each aspect of an FMI's activities is to obtain well-reasoned and independent legal opinions or analyses. A legal opinion or analysis, among other things, should identify and, where necessary, interpret the laws and regulations applicable to an FMI's operations and services.*" (p. 20, par. 3.1.4)

A/ Our first concern, (echoed by the Principle 19 on tiered participation), is the trend to establish FMIs (which are commercial entities) as regulators, not only of their direct participants but of the whole market.

FMIs would therefore become even more a Self-Regulatory Organisation, being able to regulate not only their direct participants but also the customers of the latter and so on. The quote supra is one among many expressing this ability to push own rules beyond their direct participants. The “legal basis”, putting at the same level contracts of the FMI and the applicable laws and regulations (which themselves can be “interpreted” by the counsels of the FMI) give the possibility to FMIs to edict a “rule book” which applies beyond direct participants and it appears to give a too large a margin for interpretation to the FMIs.

Considering both the systemic importance of FMIs and their commercial interest to leverage their central position in the market in order to unfairly compete with their participants, we consider that FMIs should be submitted to stringent enforcement of specific regulation and that it should be avoided that FMI could exercise discretionary regulatory powers.

B/ The second concern comes with the introduction of contracts, and hence of contractual choice of law, in the “*legal basis*” of the FMIs, at the same level and bundled with the regulatory framework.

For systemic risk reasons, it should be stated clearly that the contractual choice of law cannot be an option for the determination of the law applicable to the system and for the proprietary aspects of securities held on a participant's account in the system.

FMIs should be able to work with all their participants in the same applicable law, without introducing uncertainty (for themselves, for their participants, and for the customers of their participants) by allowing different applicable laws to be chosen in the context of each different contractual relation the FMI could enter into. In case of financial stress, the need for the FMI and its participants to sort out the diverging applicable laws which would have been introduced by the contractual choice of law would certainly deepen the crisis and put the survival of the FMI itself at risk.

Principle 2: Governance

An FMI should have governance arrangements that are clear and transparent, promote the safety and efficiency of the FMI, and support the stability of the broader financial system, other relevant public interest considerations, and the objectives of relevant stakeholders.

Key considerations

1. An FMI should have documented governance arrangements that provide clear and direct lines of responsibility and accountability. These arrangements should be disclosed to owners, relevant authorities, users, and, at a more general level, the public.
2. An FMI should have objectives that place a high priority on the safety and efficiency of the FMI and explicitly support financial stability and other relevant public interests.
3. The roles and responsibilities of an FMI’s board of directors (or equivalent) should be clearly specified, and there should be documented processes for its functioning, including processes to identify, address, and manage member conflicts of interest. The roles and responsibilities of management should also be clearly specified.

4. The board should contain suitable members with the appropriate skills and incentives to fulfil its multiple roles. This typically requires the inclusion of independent board member(s). The board should review its overall performance and that of its individual board members regularly.
5. The board should establish a clear, documented risk-management framework that includes the FMI's risk-tolerance policy, assigns responsibilities and accountability for risk decisions, and addresses decision making in crises and emergencies. Governance arrangements should ensure that the risk-management and internal control functions have sufficient authority, independence, resources, and access to the board.
6. The board should ensure that the FMI's overall strategy, rules, and major decisions reflect appropriately the interests of its participants and other relevant stakeholders. Major decisions should be clearly disclosed to relevant stakeholders and, where there is a broad market impact, the public.

This principal should not apply to SIPS which works on a cooperative mode for the industry at large. So, we would like CPSS-IOSCO to make a clear distinction between SIPS and other types of FMIs for the following reasons:

1- The existing provisions on existing CPSS Core principals are already sufficient for SIPS and so they are "well founded, clear" and have "enforceable legal basis".

2- The compliance with these core principals is regularly verified by the local overseers and the IMF which rate each SIPS and require full compliance adaptations when necessary.

3- SIPS governance is mainly in the hands of the banking industry, be it central banks for RTGSs or commercials banks for the other SIPS (eg. CHIPS in the US, Euro1 in Europe and CORE in France etc….)

In Europe SIPS settlements are only open to credit institutions in order to comply with the EU finality directive. Consequently we are not in favour of opening their boards to external independent people as the matter they treat is confidential and within the competitive area.

If principle 2 would also apply to SIPS, then it should apply to all type of SIPS irrespective of their owners (private or public sector).

As a general principle, the Associations believe that a FMI should be user-owned and user-governed with a robust governance architecture which allows the mitigation of possible conflicts of interests and which gives a central role to the risk-committee. In such architecture, the Associations do not support the possibility for independent members to participate to the FMI's board which could lead to sharing confidential information with external parties.

Principle 3: Framework for the comprehensive management of risks

An FMI should have a sound risk-management framework for comprehensively managing legal, credit, liquidity, operational, and other risks.

Key considerations

1. An FMI should have risk-management policies, procedures, and systems that identify, measure, monitor, and manage the range of risks that arise in the FMI.
2. An FMI should provide the incentives and, where relevant, the capacity to participants and their customers to manage and contain their risks.
3. An FMI should regularly review the material risks it bears from and poses to other entities (such as linked FMIs, settlement banks, liquidity providers, or service providers) as a result of interdependencies and develop appropriate risk-management tools to address these risks.

The Associations share the CPSS-IOSCO view regarding risk management.

Regarding the identification of those risks (§3.3.2), and specifically the necessity to have a "*broad-risk-management perspective",* the Associations believe that interoperability arrangements are a potential source of risk as it creates interdependencies between FMIs.

Interoperability arrangements may lead to increased systemic risk, in particular between CCPs.

Hence, even if it seems difficult to avoid such interoperability arrangements, they should be strictly controlled.

An FMI should have a risk management system in place that allows it to efficiently fulfil its role in stabilizing the market and mitigating systemic risk.

Interoperability arrangements will need careful consideration on a case-by-case basis and should be strictly controlled, given the additional risks that they may bring to the financial system.

Regarding the point 3.3.5: incentive to manage risk

We would like to add "in the same way CCP should have buy-in procedures in place as there are an efficient tool to mitigate the risk" (cf. "There are several ways in which incentives can be provided through an FMI's policies and procedures. For example, an FMI could attach financial penalties to participants that fail to settle securities in a timely manner ...")

We disagree with the idea of a loss-sharing especially when the FMI is a CCP. It could lead to an unlimited and non predetermined risk for a non defaulting participant (cf. "Another example is the use of loss-sharing arrangements based on proportionate exposures using formulas that encourage participants to manage their explicit or implicit credit exposures to one another").

Credit and liquidity risk management

Principle 4: Credit risk

An FMI should effectively measure, monitor, and manage its credit risk from participants and from its payment, clearing, and settlement processes. An FMI should maintain sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence. A CCP should also maintain additional financial resources to cover a wide range of potential stress scenarios that should include, but not be limited to, the default of the [one/ two] participant[s] and [its/their] affiliates that would potentially cause the largest aggregate credit exposure[s] in extreme but plausible market conditions.

Key considerations

1. An FMI should establish a robust framework to manage the credit risks from its participants and the credit risks involved in its payment, clearing, and settlement processes. Credit risk may arise from current exposure, potential future exposure, or both.
2. An FMI should identify sources of credit risk, routinely measure and monitor credit exposures, and use appropriate risk-management tools to control these risks.
3. A payment system, CSD, or SSS should cover its current and, where they exist, potential future exposures to each participant fully with a high degree of confidence using collateral and other equivalent financial resources (see principle 5 on collateral).
4. A CCP should cover its current and potential future exposures to each participant fully with a high degree of confidence using margin and other financial resources (see principle 6 on margin which specifies 99 percent initial margin coverage and other requirements). A CCP should also maintain additional financial resources sufficient to cover a wide range of potential stress scenarios identified in regular and rigorous stress testing that should include, but not be limited to, the default of [one/two] participant[s] and [its/their] affiliates that would potentially cause the largest aggregate credit exposure[s] in extreme but plausible market conditions.
5. A CCP should determine and test regularly the sufficiency of its financial resources by rigorous back testing and stress testing. Back testing should be conducted daily to demonstrate sufficient initial margin coverage with a 99 percent degree of confidence. Stress tests to check the adequacy of the total financial resources available in the event of a default in extreme but plausible market conditions should be performed at least monthly, or more frequently when the products cleared or markets served in general display high volatility, become less liquid, or when the size or concentration of positions held by a CCP's participants increases significantly. In addition, more routine daily or weekly stress testing in which a CCP stresses the current positions of its participants using established parameters and assumptions should be considered to be a best practice. Comprehensive stress tests, involving a full validation of models, parameters, and assumptions and reconsideration of appropriate stress scenarios, should be conducted at least annually.
6. In conducting stress testing, a CCP should consider a wide range of relevant stress scenarios, including peak historic price volatilities, shifts in other market factors such as price determinants and yield curves, multiple defaults over various time horizons, simultaneous pressures in funding and asset markets, and a spectrum of forward-looking stress scenarios in a variety of extreme but plausible market conditions. The stress-testing programme should include "reverse stress tests" aimed at identifying extreme market conditions for which the CCP's financial resources would be insufficient.
7. An FMI should have clear and transparent rules and procedures that address how potentially uncovered credit losses would be allocated, including in relation to the repayment of any funds an FMI may borrow from liquidity providers. An FMI's rules and procedures

should also indicate its process to replenish any financial resources it may employ during a stress event, including the potential default of the two participants and their affiliates that would cause the largest aggregate credit exposure so that the FMI can continue to operate in a safe and sound manner.

The Associations fully support the necessity for FMIs, as potential systemic entities, to establish a robust framework to manage credit risks entailed in their activity. In this way, diversification and intensification of different stress scenarios is necessary.

The Associations understand from Principle 4 the aim to have a conceptual framework close to the one made at a prudential level applicable to CCPs, which means that:

- the current credit exposure should be collateralized; and,

- the future credit exposure, only for CCPs, should be entirely collateralized.

Regarding those key considerations, the Associations believe they should be as consistent as possible with those currently established through the European Market Infrastructure Regulation (EMIR) or the Dodd Frank act to insure a level playing field since such rules could have important prudential impacts.

However, FMIs which are not CCPs, should be subject to a “cover one” requirement.

Another issue to be raised is linked to the use and the replenishment of financial resources (Key Consideration 7 and 3.4.15).

> "*the FMI's ability to use resources supplied by participants in one market to cover losses from a participant default in another market should have a sound legal basis, be clear to all participants, and avoid significant levels of contagion risk between markets and participants*" (3.4.15).

Even if there is a sound legal basis, it is clear that participants could lose all their assets posted to the CCP to cover the default of a participant (or a linked CCP) on a market they don't even know and combined with the possibility of “loss-sharing” this could strongly increase the risk a participant has to face.

Thus we believe that separate default funds per asset class cleared by CCPs is to be recommended.

Furthermore, with respect to Key Consideration 7, we support a waterfall procedure as proposed in the future European Market Infrastructure Regulation where margins posted by non defaulting clearing members shall not be used by a CCP to cover losses resulting from the default of another clearing member.

More generally, and as non shareholder members of FMIs (particularly for CCPs), it is important to know where exposure and replenishment obligations end, which is also linked to interoperability issues.

Collateral should be segregated so that the depositor can recover it easily in case of the depositary bankruptcy (see principle 1 on ”legal basis” and principle 16 on “Custody risk”).

This is possible if the depository is a “bankruptcy remote entity” (such as an infrastructure or the ECB).

<u>Additional comments:</u>

Regarding 3.4.14: "... *<u>market conditions that may go beyond what are considered extreme but plausible conditions</u>*": Would these conditions be disclosed? And if so, by who? This should be clarified in the report.

Principle 5: Collateral

An FMI that requires collateral to manage its or its participants' credit risk should accept collateral with low credit, liquidity, and market risk. An FMI should also set and enforce appropriately conservative haircuts and concentration limits.

Key considerations

1. An FMI should generally limit the assets it (routinely) accepts as collateral to those with low credit, liquidity, and market risk.
2. An FMI should establish prudent valuation practices and develop haircuts that are regularly tested and take into account stressed market conditions.
3. An FMI should avoid the concentration of holdings of certain assets because of potential concerns about the ability to liquidate such assets quickly without significant adverse price effects.
4. An FMI should establish stable and conservative haircuts that are calibrated to include periods of stressed market conditions in order to reduce the need for procyclical adjustments.
5. An FMI that accepts cross-border collateral should mitigate the risks associated with its use and ensure that the collateral can be used in a timely manner.
6. An FMI should have a well-designed and operationally flexible collateral management system to accommodate changes in the ongoing monitoring and management of collateral.

The Associations support the key principles regarding collateral management, i.e. the necessity:

- for a CCP to collect sufficient collateral to cover fully its participants' open positions ; and,

- for this collateral to be, as far as possible, easy to value in the event of liquidation and sufficiently acceptable to avoid credit, liquidity and market risks.

Regarding cross-border collateral (§3.5.6), the Associations support the CPSS-IOSCO analysis on the potential difficulties resulting from the different legal nature of such collateral and the potential impact of the conflict of law risk (see comments on Principle 1).

Principle 6: Margin

A CCP should cover its credit exposures to its participants for all products through an effective margin system that is risk-based and regularly reviewed.

Key considerations

1. A CCP should establish margin levels that are commensurate with the risks and unique attributes of each product, portfolio, and market it serves, taking into account potential increases in liquidation times in stressed markets.
2. A CCP should have a reliable source of timely price data for its margin models and regular collection of variation margin. A CCP should also have procedures and sound valuation models for addressing circumstances where pricing data is not readily available or reliable. As an input for its initial margin models, a CCP should rely upon pricing data covering an appropriate historical time period for the products it clears.
3. A CCP should adopt initial margin models and parameters that are risk-based and generate margin requirements sufficient to cover potential future exposure to participants in the interval between the last margin collection and the close out of positions following a participant default. Initial margin should meet an established single-tailed confidence level of at least 99 percent for each product that is margined on a product basis, each spread within or between products for which portfolio margining is permitted, and for each clearing member's portfolio losses. The model should also be based on adequate time horizons for the close out of the particular types of products cleared by the CCP, have an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products, and, to the maximum extent practical and prudent, avoid the need for destabilising, procyclical changes.
4. At least daily, a CCP should mark participant positions to market and collect variation margin to limit the build-up of current exposures. A CCP should have the authority and operational capacity to make intraday calls for initial and variation margin from participants with positions that have lost significant value.
5. In calculating margin requirements, a CCP may allow offsets or reductions in required margin across products that it clears or between products that it and another CCP clear, if the price risk of one product is significantly and reliably correlated with the price risk of the other product. Where two or more CCPs are authorised to offer cross-margining, they must have appropriate safeguards and harmonise their overall risk-management programmes.
6. A CCP should analyse and monitor its model performance and overall margin coverage by conducting rigorous daily back testing and at least monthly, if not more frequent, stress testing. A CCP should regularly conduct an assessment of the theoretical and empirical properties of its margin model for all products it clears. A CCP, in reviewing its model's coverage, should take into account a range of scenarios, including scenarios that capture the most-volatile periods that have been experienced by the markets it serves and develop forward-looking scenarios to anticipate risks.
7. A CCP should regularly review and validate its margin system.

The Associations broadly support the key considerations developed under this Principle.

However, the Associations would like to make the following comments:

- the distinction between initial margin and default funds doesn't clearly appear through the wording of key consideration 1;

- key consideration 6 seems to use stress testing to analyse margin coverage. Such consideration should be nuanced since margin coverage is used to address credit

risk in normal conditions, not to monitor stress scenarios. The future European regulation (EMIR, article 39) is built in that way.

Principle 7: Liquidity risk

An FMI should effectively measure, monitor, and manage its liquidity risk. An FMI should maintain sufficient liquid resources to effect same-day and, where appropriate, intraday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of [one/two] participant[s] and [its/their] affiliates that would generate the largest aggregate liquidity need in extreme but plausible market conditions.

Key considerations

1. An FMI should have a robust framework to manage its liquidity risks from its participants, settlement banks, nostro agents, custodian banks, liquidity providers, and other entities.
2. An FMI should have effective operational and analytical tools to identify, measure, and monitor its settlement and funding flows on an ongoing and timely basis, including its use of intraday liquidity.
3. An FMI should maintain sufficient liquid resources (that is, liquid assets and prearranged funding arrangements) to effect same-day and, where appropriate, intraday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the [one/two] participant[s] and [its/their] affiliates that would generate the largest aggregate liquidity need in extreme but plausible market conditions. A payment system, CSD, or SSS, including one employing a DNS mechanism, should have sufficient liquid resources to effect, at a minimum, timely completion of daily settlement in the event of the inability of the [one/two] participant[s] and [its/their] affiliates with the largest aggregate payment obligation[s] to settle those obligations. A CCP should have sufficient liquid resources to meet required margin payments and effect the same-day close out or hedging of the [one/two] participant[s] and [its/their] affiliates with the largest potential liquidity need[s] in extreme but plausible market conditions.
4. An FMI should obtain a high degree of confidence through rigorous due diligence that each liquidity provider, whether or not it is a participant of the FMI, would have sufficient information to understand and to manage its associated liquidity risks, and that it has the capacity to perform as required under the liquidity arrangement. Where relevant to assessing a liquidity provider's performance reliability with respect to a particular currency, a liquidity provider's potential access to credit from the central bank of issue should be taken into account. An FMI should regularly test access to its liquid resources at a liquidity provider.
5. For the purposes of this principle, liquid resources include cash at the central bank of issue and creditworthy commercial banks, as well as highly marketable collateral held in custody and investments that are readily available on a same-day basis and that are also convertible into cash with prearranged funding arrangements including committed liquidity lines, foreign exchange swaps, repos, or pledges. If an FMI has access to central bank credit, then an appropriate portion of its collateral holdings should be eligible for pledging to (or conducting other appropriate forms of transactions with) the relevant central bank. An FMI should not assume the availability of emergency central bank credit as a part of its liquidity plan.
6. If an FMI has access to central bank accounts, payment services, or securities services, the FMI should use these services, where practical and available, to enhance its management of liquidity risk.
7. An FMI should determine and test the sufficiency of its liquid resources by regular and rigorous stress testing. An FMI should have clear procedures to use the results of its stress test and to evaluate and adjust the adequacy of its liquidity risk-management framework. In conducting stress testing, an FMI should consider a wide range of relevant scenarios,

including peak historic price volatilities, shifts in other market factors such as price determinants and yield curves, multiple defaults over various time horizons, simultaneous pressures in funding and asset markets, and a spectrum of forward-looking stress scenarios in a variety of extreme but plausible market conditions. Scenarios should also consider the design and operation of the FMI, and include all entities that might pose material liquidity risks to the FMI (such as settlement banks, nostro agents, custodian banks, liquidity providers, and linked FMIs). The stress-testing programme should include "reverse stress tests" aimed at identifying extreme market conditions for which the FMI's liquid resources would be insufficient.
8. An FMI should have clear and transparent rules and procedures to address unforeseen and potentially uncovered liquidity shortfalls in order to avoid unwinding, revoking, or delaying the same-day settlement of payment obligations. An FMI's rules and procedures should also indicate its process to replenish any liquidity resources it may employ during a stress event, including the default of the two participants and their affiliates that would potentially cause the largest combined liquidity needs, so that it can continue to operate in a safe and sound manner.

First of all, the Associations welcome developments on liquidity risks for CCPs.

In their response on the 2010's consultative report on "*Recommendation for Central Counterparties to OTC Derivatives CCPs"*, the Associations already underlined their belief that a CCP should always be in a position to rapidly and securely obtain the necessary liquidity provided by the central bank, to limit systemic risk.

In the event of a severe financial crisis, central banks have a major role to play in order to solve the crisis. In case of default of one of its participants, the CCP needs to be able to access to the liquidity provided by a central bank as rapidly as possible (on an intraday or overnight basis).

In this context, the CCP must have a direct link with the central bank which seems difficult if it is not under its supervision.

This is the reason why the Associations have always supported the necessity for a FMI, as far as possible, to have a banking status limited to its activity.

Besides, we understand from this principle and its key considerations that it is not currently decided whether such liquidity risk framework should be made on the hypothesis of the default of one or two participants. Concerning the future European regulation on market infrastructure, such hypothesis is currently based on the default of two clearing members.

Furthermore, with respect to Key Consideration 8, we support a waterfall procedure as proposed in the future European Market Infrastructure Regulation where margins posted by non defaulting clearing members shall not be used by a CCP to cover losses resulting from the default of another clearing member.

In the case of payment systems, the prime requirement should be that the FMI ensures that only high quality and liquid collateral with appropriate haircuts is used. **On this basis the Associations suggest that settlement risk in payment systems is treated as liquidity risk and not as credit risk.**

Liquidity risk will remain with the participants either directly or through some form of common collateral or liquidity pool. The payment system's responsibility is to implement rules and procedures ensuring that adequate liquidity/collateral is available for settlement.

Subject to the conditions listed below, "cover one" should be the minimum requirement for payment systems. A major reason for this is the likely limit on the availability of suitable collateral which may also be required for a range of other purposes including Basel regulatory requirements, monetary policy operations and other FMIs. Our concern is that stipulating a minimum "cover two" requirement could result in some institutions relying on other participants' liquidity by delaying outward payments which would not only reduce operational efficiency but also potentially create additional risk for the other participants who may effectively be acting as unsecured liquidity providers.

However, this proposal is subject to the following conditions.

- Group situations where participants are financially linked are treated as one participant for this purpose and the phrase "participant and its affiliates" is not considered sufficiently explicit. Instead, it should be replaced with more formal group criteria, possibly based on Basel principles. It follows that several participants (and their affiliates) may be counted as a single entity for "cover one" purposes.

- When applying this requirement, it must be possible for payment systems to measure and control the highest intra-day credit risk, where applicable, and this requirement should be applied to such risk. For DNS systems, the term "intra-day" should be construed as being the highest credit risk arising during the deferred settlement process based on the underlying legal infrastructure. It is acknowledged that some payment systems may require time to accommodate this requirement but it is considered important that the underlying principle should be established.

- Robust default procedures , including where two or more participants fail simultaneously, with mandatory testing at least annually and more frequently if material changes are made, should be put in place so that in a crisis situation they can be implemented without delay.

As mentioned above, consistency should be reached with both EU and US regulation.

Settlement

Principle 8: Settlement finality

An FMI should provide clear and certain final settlement, at a minimum, by the end of the value date. Where necessary or preferable, an FMI should provide final settlement intraday or in real time.

Key considerations

1. An FMI should clearly define the point at which the settlement of a payment, transfer instruction, or other obligation is irrevocable and unconditional.
2. An FMI should complete final settlement no later than the end of the value date, and preferably intraday or in real time, to reduce settlement risk. An LVPS, CSD, or SSS should consider adopting RTGS or multiple-batch processing during the settlement day.
3. An FMI should clearly define the point in time before settlement when unsettled payment or transfer instructions or obligations may not be revoked.

Settlement finality is the corner stone of a safe settlement process and hence, a major component of systemic stability.

There should be only one system providing settlement finality for any given transaction. This issue is not addressed in the Report.

However, in paragraph 3.8.6 *"revocation of transfer instructions"*, the words "*or discourage*" should be deleted as settlement rules should be clearly defined, in particular where a stress situation occurs.

Principle 9: Money settlements

An FMI should conduct its money settlements in central bank money where practical and available. If central bank money is not used, an FMI should minimise and strictly control the credit and liquidity risk arising from the use of commercial bank money.

Key considerations

1. An FMI should conduct its money settlements in central bank money, where practical and available, to avoid credit and liquidity risks.
2. If central bank money is not used, an FMI should conduct its money settlements using a settlement asset with little or no credit or liquidity risk.
3. An FMI that settles in commercial bank money should establish and monitor adherence to strict criteria for its settlement banks that take account of, amongst other things, their supervision, creditworthiness, capitalisation, access to liquidity, and operational reliability.
4. An FMI should closely control the credit and liquidity risks from its commercial settlement banks, including the distribution of exposures among its commercial settlement banks.
5. If an FMI conducts money settlements on its own books, it should minimise and strictly control its credit and liquidity risks.

In Key consideration 1, *"An FMI should conduct its money settlements in central bank money where practical and available",* the word "*practical*" could be misleading in that turning to central bank money would depend on a commercial or organizational convenience.

"*Practical*" should be (by preference) omitted or replaced by "*feasible in practice*".

Furthermore, the Associations strongly believe that a CCP shall have access to central bank facilities, in order to avoid any contagion in case of failure of a clearing member.

Thus, they shall have a banking status or an *ad hoc* banking-like status, since the central banks do not accept any access to the overnight liquidity for non banking entities.

This does not only involve a banking status or *ad hoc* banking-like status for CCPs, but also that it would not be possible for any stakeholder which does not have such status to become a FMI.

It should be kept in mind that a banking or banking-like status also means that the FMI has to be supervised and monitored also by a banking supervisor, including on-site audit inspections.

As the Associations have always stressed, they strongly believe that a FMI should always be in a position to rapidly and securely obtain the necessary liquidity for it to limit systemic risk, as provided by the central bank.

In the event of a major financial crisis, central banks have a major role to play in order to solve the crisis.

In case of default of one of its participants, a FMI needs to be able to access the liquidity provided by a central bank as rapidly as possible. In this context, the FMI shall have a direct link with the central bank which seems difficult if it is not under its supervision.

Principle 10: Physical deliveries

An FMI should clearly state its obligations with respect to the delivery of physical instruments or commodities and should identify, monitor, and manage the risks associated with such physical deliveries.

Key considerations

1. An FMI's rules should clearly state its obligations with respect to the delivery of physical instruments or commodities.
2. An FMI should identify, monitor, and manage the risks associated with the storage and delivery of physical instruments or commodities.

The Associations support this Principle 10.

Central securities depositories and exchange-of-value settlement systems

Principle 11: Central securities depositories

A CSD should have appropriate rules and procedures to help ensure the integrity of securities issues and minimise and manage the risks associated with the safekeeping and transfer of securities. A CSD should maintain securities in an immobilised or dematerialised form for their transfer by book entry.

Key considerations

1. A CSD should have appropriate rules and procedures, including robust accounting practices and controls, to safeguard the interests of securities issuers and holders, prevent the unauthorised creation or deletion of securities, and conduct periodic reconciliation of securities issues it maintains.
2. A CSD should prohibit overdrafts or debit balances in securities accounts.
3. A CSD that maintains a link to another CSD should prohibit the provisional transfers of securities or, at a minimum, prohibit the retransfer of securities prior to the first transfer becoming final.
4. A CSD should maintain securities in an immobilised or dematerialised form for their transfer by book entry. Where appropriate, a CSD should provide incentives to immobilise or dematerialise securities.
5. A CSD should identify, measure, monitor, and manage its risks from other activities that it may perform; additional tools may be necessary in order to address these spillover effects.

6. A CSD providing central safekeeping and settlement services to a CCP should ensure that the CCP would not pose additional material risks (such as liquidity and operational risk) as compared to any other participant in the CSD and, where necessary, take additional measures.

CSDs in most countries maintain the securities accounts of their participants in the context of their activity of reconciliation between the issuers' account on the one hand and the participants' accounts on the other , thus ensuring that the number of securities in circulation is equal to the number issued. Therefore we would like to:

- see the definition as follows: "*A central securities depository ensures the integrity of the system by reconciliating the number of securities issued and registered in the issuers' accounts with the number of securities maintained in the securities accounts of its participants".*

- also have the first sentence of Key Consideration 4 *" A CSD should maintain securities in an immobilised or dematerialised form for their transfer by book entry "* redrafted as follows *: "A CSD should maintain securities accounts for its participants to which securities are credited either in physical form or in dematerialized form".*

As already stated[3] the role of a CSD is to safeguard the interests of securities issuers and holders. This means that a CSD should offer no activity that could increase the risk it could face especially when such activity could be done by others means. For example, the document points out the risk to which a CSD could be exposed when acting as principal in a security lending transaction (potential need to acquire the lent securities). This should be sufficient to say that a CSD should limit its activity to its core functions (aiming at a low-risk profile).

As a consequence, should a company operating as CSD be willing to engage in non CSD services, it should be subject to a mandatory "2+2" model, whereby different licenses should be applied for by different entities, so that CSD functions are performed by a regulated entity that is not engaged in other activities (such as credit provision of credit and of issuers services)..

In this respect, the Associations propose that, in paragraph 3.11.6, the sentence "*Additional tools may be necessary to address these risks, or the FMI may need to separate legally to other activities"* be modified as follow*:* "*Additional tools ~~may~~* ***should*** *be necessary to address these risks, ~~or~~* ***and*** *the FMI ~~may~~* ***will*** *need to ~~separate~~ legally segregate ~~to other~~* ***the different*** *activities".*

Finally, regarding registrars that are excluded from the scope of this consultation though they have a role related to the integrity of the issuance, we suggest that if they still perform this function, the responsibility of the integrity of the issuance should be guaranteed by the domestic CSD (as it is one of the core services defining a CSD) and that most of the securities should benefit from the safety provided by the central recording by a CSD.

[3] see General Remarks

Principle 12: Exchange-of-value settlement systems **If an FMI settles transactions that involve the settlement of two linked obligations (for example, securities or foreign exchange transactions), it should eliminate principal risk by conditioning the final settlement of one obligation upon the final settlement of the other.** ***Key considerations*** *1. An FMI that is an exchange-of-value settlement system should eliminate principal risk by linking the final settlement of one obligation to the final settlement of the other.* *2. The settlement of two obligations can be achieved in several ways and varies by how trades or obligations are settled, either on a gross basis (trade-by-trade) or on a net basis, and the timing of when finality occurs.*

The Associations fully support this Principle 12.

Default management

Principle 13: Participant-default rules and procedures **An FMI should have effective and clearly defined rules and procedures to manage a participant default that ensure that the FMI can take timely action to contain losses and liquidity pressures, and continue to meet its obligations.** ***Key considerations*** *1. An FMI should have default rules and procedures that enable the FMI to continue to meet its obligations in the event of a participant default and that address the replenishment of resources following a default.* *2. An FMI should be well prepared to implement its default rules and procedures, including the exercise of any appropriate discretionary procedures provided in its rules.* *3. An FMI should make key aspects of its default rules and procedures available to the public.* *4. An FMI should engage with its participants and other relevant stakeholders in the periodic testing and review of its default procedures to ensure that they are practical and effective.*

The Associations support Principle13 and its key considerations.

The future European regulation on market infrastructure may mention in addition of those considerations that a CCP “shall promptly inform the competent authority” where it considers that a clearing member will not be able to meet its future obligations and before it declares its default. This is an important provision as most of FMIs (like CCPs) have a systemic importance.

The use of the resources by a CCP when a participant defaults is not clear (3.13.3). We would like to push for more requirements. The default waterfall principle as proposed in the European Market Infrastructure Regulation (article 42) seems to be an appropriate approach for such CCPs.

Principle 14: Segregation and portability

A CCP should have rules and procedures that enable the segregation and portability of positions and collateral belonging to customers of a participant.

Key considerations

1. A CCP should have segregation and portability arrangements that protect customer positions and collateral to the greatest extent possible under applicable law, particularly in the event of a default or insolvency of a participant.
2. A CCP should employ an account structure that enables it readily to identify and segregate positions and collateral belonging to customers of a participant. Such CCPs should maintain customer collateral and positions in an omnibus account or in individual accounts at the CCP or at its custodian.
3. A CCP should structure its arrangements in a way that facilitates the transfer of the positions and collateral belonging to customers of a defaulting participant to one or more other participants.
4. A CCP should clearly disclose its rules, policies, and procedures relating to the segregation and portability of customer positions and collateral. In addition, a CCP should disclose any constraints, such as legal or operational constraints, that may impair its ability fully to segregate or port customer positions and collateral.

It is the Associations opinion that segregation and portability arrangements are of utmost importance to ensure the protection of customers and their positions in case of a participant's default.

We then support the key considerations developed in Principle 14.

However, as far as we understand the various types of possible segregation arrangements, the US (through the Dodd Frank Act) and the EU (through EMIR) legislations currently discussed will impose their own levels of segregation, each with their own consequences (including prudential consequences). In its December 2010 consultative document on "*Capitalisation of bank exposures to central counterparties*" the Basel Committee proposes a favourable treatment for 'bankruptcy-remote' collateral for clearing members as well as the favourable risk weight for qualifying CCPs for non-member banks exposures provided their assets are segregated and bankruptcy-remote from the clearing member. We would like to draw the Committee's attention that the concept of bankruptcy-remote collateral is not aligned with the CCPs' various segregation models prevailing today and relies too much on national bankruptcy laws which are far from being aligned. In addition, our understanding is that the concept of "bankruptcy remote" is only relevant for securities, cash being commingled. Therefore, the Associations suggested in their response to the consultative document to base the most favourable treatment on a notion of "*appropriate segregation*" as the current legislation both in the EU and in the US are about to precisely define the level of segregation expected from CCPs.

Furthermore, this Principle should provide a clear definition of "customers" since many types of customers exist. Is it the Trading Member Firm (TMF)? The client of the TMF? Indeed most often it is up to the CMF (the CCP's participant) to post collateral and to require collateral from its customers. Acting solely as a TMF, the GCM's customer could then in turn ask its own customers to provide collateral to cover their open positions. Then, in the books of the TMF as well as in those of the GCM or of the CCP there are accounts reflecting the amount and the ownership of each deposit. The aim of Principle 14 is to protect the positions/collateral of a customer of a participant by using "an account structure that enables

it …/… to identify and segregate positions and collateral belonging to customers of a participant". That said, who should be the owner of the account in the CCP's books? The customer of the participant or the owner of the collateral?

Re-hypothecation of non-cash collateral provided to an FMI should be prohibited as it would create additional types of risk, thus limiting the purpose of collateral as a means to reduce counterparty and market risks.

It is our opinion that securities collateral should be segregated and cash collateral should be held with the relevant central bank.

General business and operational risk management

Principle 15: General business risk

An FMI should identify, monitor, and manage its general business risk and hold sufficiently liquid net assets funded by equity to cover potential general business losses so that it can continue providing services as a going concern. This amount should at all times be sufficient to ensure an orderly wind-down or reorganisation of the FMI's critical operations and services over an appropriate time period.

Key considerations

1. An FMI should have robust management and control systems to identify, monitor, and manage general business risks, including business strategy, cash flows, and operating expenses.
2. An FMI should hold sufficient equity or equity capital, in the form of shareholders' funds (such as common stock, disclosed reserves, or retained earnings), to cover potential general business losses, so that it can continue providing services as a going concern. Resources held to cover potential general business losses should be in addition to resources held to cover participant defaults or other risks covered under financial resource principles.
3. At a minimum, an FMI should hold equity capital at normal times equal to [six, nine, or twelve] months of expenses. An FMI may also need to hold additional equity capital, taking into account its general business risk profile. Capital held under international risk-based capital standards should be included where relevant and appropriate to avoid double regulation.
4. In addition to capital adequacy, an FMI's equity capital should reflect a strong cash, cash-equivalent, or securities position to allow the FMI to meet its current and projected operating expenses under a range of scenarios; cash equivalents and securities should consist of high-quality and sufficiently liquid assets that can easily be converted into cash at little or no loss of value, even in adverse market conditions.
5. An FMI should maintain a viable plan for (a) raising additional capital should its equity capital approach or fall below the minimum; and (b) if the FMI is unable to raise new capital, achieving an orderly wind down or reorganisation of its operations and services. This plan should be approved by the board of directors (or an appropriate board committee), updated regularly, and reviewed by the FMI's regulator, supervisor, or overseer.

The Associations would like to remind that minimum amount proposed by EMIR for a CCP is 10 millions Euros.

Regarding operating expenses (question 11), quantitative requirement should be equal to 6 months of operating expenses. However, such provision is not relevant for cash settlement activities.

Principle 16: Custody and investment risk

An FMI should safeguard its assets and minimise the risk of loss or delay in access to those assets, including assets posted by its participants. An FMI's investments should be in instruments with minimal credit, market, and liquidity risks.

Key considerations

1. An FMI should hold its assets, including assets that its participants have posted to it, at supervised and regulated entities that have robust accounting practices, safekeeping procedures, and internal controls that fully protect these assets.
2. An FMI should have prompt access to its assets, including assets posted by participants, when required.
3. An FMI's investment strategy should be consistent with its overall risk-management strategy, and investments should be secured by, or be claims on, high-quality obligors. These investments should allow for quick liquidation with little, if any, adverse price effect.

If a commercial bank is used as custodian, the assets held under custody are guaranteed to a specific threshold which is not relevant for the amounts posted for collateral or margin purposes. The participant may get back assets posted in the books of the defaulting bank but has no certainty on if it would be the whole amount.

The Associations believe that such assets should benefit from a safe keeping related to their role (i.e.: in a NCB or a CSD).

Principle 17: Operational risk

An FMI should identify all plausible sources of operational risk, both internal and external, and minimise their impact through the deployment of appropriate systems, controls, and procedures. Systems should ensure a high degree of security and operational reliability, and have adequate, scalable capacity. Business continuity plans should aim for timely recovery of operations and fulfilment of the FMI's obligations, including in the event of a wide-scale disruption.

Key considerations

1. An FMI should establish a robust operational risk-management framework with appropriate systems, policies, procedures, and controls to identify, monitor, and manage operational risks.
2. The roles and responsibilities for operational risk should be clearly defined within the FMI, and the FMI's operational risk-management framework should be endorsed by the FMI's board of directors. Risks, operational policies and procedures, and systems should be reviewed, audited, and tested periodically and after significant changes.
3. An FMI should have clearly defined operational reliability objectives and should have policies in place that are commensurate with those objectives. An FMI should have adequate capacity and scalability, as well as the tools and procedures to monitor the performance of the FMI.

4. An FMI should have well-defined physical and information security policies. All potential vulnerabilities and threats should be investigated, assessed, and documented.
5. An FMI should have a business continuity plan that addresses events posing a significant risk of disrupting operations, including events that could cause a wide-scale disruption. The plan should incorporate the use of a secondary site and should ensure that critical information technology (IT) systems can resume operations within two hours following disruptive events. In case of extreme circumstances, settlement should be ensured by the end of the day at the latest. The FMI should plan and carry out a programme of tests of these arrangements.
6. An FMI should identify, monitor, and manage the risks that key participants, other FMIs, and service and utility providers might pose to its operations. In addition, an FMI should identify, monitor, and manage the risks its operations might pose to other FMIs.

The Associations support this Principle 17.

Access

Principle 18: Access and participation requirements

An FMI should have objective, risk-based, and publicly disclosed criteria for participation, which permit fair and open access.

Key considerations

1. An FMI should allow for fair and open access to its services, including by direct and, where relevant, indirect participants and other FMIs, based on reasonable risk-related participation requirements.
2. Any restrictions in an FMI's participation requirements should be justified in terms of the safety and efficiency to the FMI and the markets it serves, be tailored to its specific risks, and be publicly disclosed.
3. An FMI should monitor compliance with its participation requirements on an ongoing basis, and have clear procedures for facilitating the suspension and orderly exit of a participant that breaches, or no longer meets, the participation requirements.

Access requirements need to be objective, non-discriminatory and publicly disclosed to provide open participation to market participants, market infrastructures, trading venues and service providers.

Access should only be restricted where this would pose a risk to the efficient and safe functioning of an FMI.

Such principals already apply to payments Market Infrastructure (SIPS and other) that issue clear and secured rules concerning access criteria. Such a transparency has two main sources: the competition authorities who require to give fair and equal access to all the authorized competitors as direct participants and the central banks who have a close control on payments/settlement security.

Regarding CCPs they will need to establish processes to connect with different market infrastructures so that open access and efficient operational risk management is guaranteed.

Principle 19: Tiered participation arrangements

An FMI should, to the extent practicable, identify, understand, and manage the risks to it arising from tiered participation arrangements.

Key considerations

1. An FMI should, to the extent practicable, identify, understand, and manage its potential risks arising from such tiered participation arrangements. The risks identified and the proposed mitigating actions should be reported to the FMI's board of directors.
2. An FMI should ensure that its rules and procedures for direct participants allow it to gather basic information about indirect participation and to identify, monitor, and manage relevant concentrations of risk and important interdependencies. To the extent possible, an FMI should seek to identify direct participants acting on behalf of a material number of indirect participants, indirect participants with significant daily turnover in the system, indirect participants that are larger than the direct participants through which they access the FMI or that pose other specific risks.
3. If an FMI identifies material risks arising from tiered participation arrangements, it should periodically review the system rules and procedures with its board to determine whether there are potential issues related to indirect participation in terms of legal structure, finality, or the stable operation of the system, and ensure that the nature of each user's participation is clearly defined.

We understand the motivation for this principle. However, we believe that it would be difficult for an FMI to identify, understand and manage the risks arising from indirect participants.

Indeed, when within the payments industry there are clearly two types of Market Infrastructure (FMIs with a single participation circle[4] and FMIs with two participation circles[5]), it is not the case for all others.

For CCPs, for example, we need once again to determine who the client is. The one which executes the order on a market (*i.e.* TMF[6])? The one which wants to buy/sell? Even if the CCP is authorised to get information about the "client", how would this information be used? How would the CCP determine if there is a risk on this client or not? And what could it do then? Ask the participant to stop working with its client? Increase the margin requirements?

The same difficulties may arise for CSDs. How could they get information on customers from participants where they could be their competitors in providing custody service?

Considering the FMI conflicts of interests, we strongly oppose conferring regulatory and enlarged supervisory functions to FMIs which would go beyond their direct participants. This trend appears clearly especially in Principle 19 ("Tiered participation arrangements"), and as well in Principle 1 ("Legal basis"). Principle 19 confers upon the FMI regulatory powers on all market participants, while Principle 1 seems to create a new "rule book" for the whole market where the rules of the FMIs are bundled together (and put as the same level) with laws and regulations promulgated by the regulators. In this respect, in paragraph 3.1.4 of Principle 1, using the verb « *interpret* » in the sentence « *A legal opinion or analysis, among other things,*

[4] *Where the other banks are simple clients of the direct participants. The clients are not legally part of the market infrastructure, so they are not concerned by principle 19*
[5] *Where the indirect participants are officially recognized by the system and as such are concerned by principle19*
[6] Trading Member Firm

should identify and, where necessary, ***interpret*** *the laws and regulations applicable to an FMI's operations and services*" is misleading.

FMIs can legitimately rule their relationship with their direct participants, provided that these rules would be uniform, public (transparent) and approved by the regulator/supervisor. But the negative externalities, in term both of systemic risk and fair competition, of giving regulatory powers to the FMIs on the whole market, by far exceed the potential advantages

For these reasons, this Principle 19 should be deleted.

Principle 20: FMI links

An FMI that establishes a link with one or more FMIs should identify, monitor, and manage link-related risks.

Key considerations

1. Before entering into a link arrangement and on an ongoing basis once the link is established, an FMI should identify and assess all potential sources of risk arising from the link arrangement. Link arrangements should be designed such that each FMI is able to observe the other principles in this report.
2. A link should have a well-founded legal basis, in the relevant jurisdictions, that supports its design and provides adequate protection to the FMIs in the operation of the link.
3. Linked CSDs should measure, monitor, and manage their credit and liquidity risks arising from each other. Any credit extensions between CSDs should be covered fully with high-quality collateral and be subject to limits.
4. Provisional transfers of securities between linked CSDs should be prohibited or, at a minimum, the retransfer of provisional transferred securities should be prohibited prior to the transfer becoming final.
5. An investor CSD should only establish a link with an issuer CSD if the arrangement provides a high level of protection for the rights of the investor CSD's participants.
6. An investor CSD that uses an intermediary to operate a link with an issuer CSD should measure, monitor, and manage the additional risks (including custody, credit, and operational risks) arising from the use of an intermediary.
7. Before entering into a link with another CCP, a CCP should identify the potential spillover effects of the linked CCP's default and assess its ability to cope with such occurrence. If a link has three or more CCPs, each CCP should identify, assess, and manage the risks of the collective links arrangement.
8. The inter-CCP risk management for the provision and holding of financial resources should enable each CCP to cover at least on a daily basis its current exposures fully and its potential future exposure with a high degree of confidence, without reducing the CCP's ability to fulfil its own obligations at any time.
9. A TR should carefully assess the additional operational risks related to its links to ensure the scalability and reliability of IT and related resources.

We understand that CPSS-IOSCO consider interoperability between FMIs, especially when they are CCPs.

As already mentioned, the Associations do not support interoperability arrangements for the following reasons.

First of all, implementation of interoperability is difficult, as evidenced by the fact that, in the European area, after about 4 years of work done by the banking and financial industry and monitoring of the Code of Conduct by the European Commission, interoperability links have not yet been implemented, despite multiple demands. Since the market infrastructures have published access and interoperability guidelines, more than 80 demands have been issued but none has as yet been put in place.

This is due to, amongst others, the following reasons:

- The complexity of building interoperability links between CCPs due to obstacles that prevent competition on an equal footing ;

- The multiple differences that exist for the respective CCPs, representing public sector barriers: differences in national, legal requirements and some regulatory obstacles brought forward by regulators and supervisors; as well as private sector barriers ;

- Players have realized that answering to all requests for access and interoperability would result in a spaghetti network.

Secondly, the development of interoperability between CCPs could lead to a propagation of systemic risk between interconnected CCPs, which leads to the opposite result envisaged by the clearing of OTC derivatives.

To conclude, even if it seems difficult to avoid such interoperability arrangements, they should be strictly controlled.

Any links regarding post-trade infrastructures and other third-party service providers will need to be closely monitored to mitigate any operational and legal risk.

Communication systems and procedures should be secure to enable efficient interconnectivity

Efficiency

Principle 21: Efficiency and effectiveness

An FMI should be efficient and effective in meeting the requirements of its participants and the markets it serves.

Key considerations

1. An FMI should be designed to meet the needs of its participants and the markets it serves, in particular, with regard to choice of a clearing and settlement scheme; operating structure; scope of products recorded, cleared, or settled; and use of technology and procedures.
2. An FMI should have clearly defined goals and objectives that are measurable and achievable, such as in the areas of minimum service levels, risk-management expectations, and business priorities.
3. An FMI should have established mechanisms for the regular review of its efficiency and effectiveness.

The Associations support this Principle 21.

Principle 22: Communication procedures and standards

An FMI should use or accommodate the relevant internationally accepted communication procedures and standards in order to facilitate efficient recording, payment, clearing, and settlement across systems.

Key considerations

1. An FMI should use, or at a minimum accommodate the use of, internationally accepted communication procedures that can support interoperability between the FMI, its participants, their customers, and other users (such as third-party service providers and other FMIs).
2. An FMI should use, or at a minimum accommodate, internationally accepted communication standards, such as standardised messaging formats and reference data standards for identifying financial instruments and counterparties.
3. An FMI that operates across borders should use, or at a minimum accommodate, internationally accepted communication procedures and standards.

With respect to the principle of interoperability, see our comments under Principle 20.

We strongly believe that protocols and standards issues should be kept at "scheme" level and surely not at a messaging or technical level. In addition as far as communication protocols and networks are concerned we would like the regulators to insure a real level playing field between the different solutions.

Transparency

Principle 23: Disclosure of rules and procedures

An FMI should have clear and comprehensive rules and procedures and should provide sufficient information to enable participants to have an accurate understanding of the risks they incur by participating in the FMI. All relevant rules and key procedures should be publicly disclosed.

Key considerations

1. An FMI should adopt clear and comprehensive rules and procedures that are fully disclosed to participants and relevant rules and key procedures should be publicly disclosed.
2. An FMI should disclose clear descriptions of the system's design and operations, as well as the rights, obligations, and risks participants incur by participating in the FMI.
3. An FMI should provide all necessary and appropriate documentation and training to facilitate participants' understanding of the FMI's rules and procedures and the risks they face from participating in the FMI.
4. An FMI should publicly disclose its fees at the level of individual services it offers, as well as its policies on any available discounts. The FMI should provide clear descriptions of priced services for comparability purposes.

The Associations agree with Principle 23 and its key considerations if a real level playing field is insured by the different regulators when implementing this principle.

Principle 24: Disclosure of market data

A TR should provide timely and accurate data to relevant authorities and the public in line with their respective needs.

Key considerations

1. A TR should provide data in line with regulatory and industry expectations to relevant authorities and the public, respectively, that is comprehensive and at a level of detail sufficient to enhance market transparency and support other public policy objectives.
2. A TR should have effective processes and procedures to provide data to relevant authorities in a timely and appropriate manner to enable them to meet their respective regulatory mandates and legal responsibilities.
3. A TR should have robust information systems that provide accurate current and historical data. Data should be provided in a timely manner and in a format that permits it to be easily analysed.

While the Associations fully support the provision of timely and accurate data by Trade Repositories (TRs) to relevant public authorities, effective access by the public to the data recorded in TRs must be assessed carefully in the context of the impact this may have on market liquidity. Therefore, even if only aggregated breakdowns and anonymous data are being provided, the phrase "*as available and appropriate to the public*" (3.24.2) should be duly considered when seeking for greater transparency to the broader public.

Responsibilities of central banks, market regulators, and other relevant authorities for financial market infrastructures

As stated in 1.28, "*While each individual FMI is fundamentally responsible for complying with these principles, effective regulation, supervision, and oversight are necessary to ensure compliance and induce change*" so we welcome the Section 4 which "*encourages authorities to pursue effective regulation, supervision, and oversight; regulatory transparency; and the adoption and consistent application of the principles*".

For this reason, we believe that these Responsibilities should be more stringent and that Principles / Responsibilities need to be added on the duties of legal authorities to ensure that regulators, supervisors and overseers have the means to fully exercise all these responsibilities and are clearly independent from the owner of the FMI. The aim of this new set of Principles could be reached only if all the levels are clearly involved.

Finally, as stated above for Principles there should be no distinction between privately or publicly owned/operated FMIs. We then believe that Responsibilities should reflect it and we strongly ask CPSS IOSCO to review them so that it would be clear that the duties of regulators, supervisors or overseers are the same irrespective of who owns / operates the FMI.

***Responsibility A: Regulation, supervision, and oversight of FMIs* should be subject to appropriate and effective regulation, supervision, and oversight by a central bank, market regulator, or other relevant authority.**

Key considerations

1. Authorities at the national level should publicly disclose the criteria used to identify FMIs that should be subject to regulation, supervision, and oversight.
2. FMIs that have been identified using these criteria should be regulated, supervised, and overseen by appropriate authorities such as a central bank, market regulator, or other relevant body.

See above

***Responsibility B: Regulatory, supervisory, and oversight powers and resources* Central banks, market regulators, and other relevant authorities should have the powers and resources to carry out effectively their responsibilities in regulating, supervising, and overseeing FMIs.**

Key considerations

1. Authorities should have specific powers or other authority consistent with their relevant responsibilities, including the ability to obtain information and induce change.
2. Authorities should have sufficient resources to fulfil their regulatory, supervisory, and oversight responsibilities.

See above

***Responsibility C: Disclosure of objectives and policies with respect to FMIs* Central banks, market regulators, and other relevant authorities should clearly define and disclose their regulatory, supervisory, and oversight policies with respect to FMIs.**

Key considerations
1. Authorities should clearly define their policies with respect to FMIs, which include the authorities' objectives, roles, and regulations.
2. Authorities should publicly disclose their relevant policies in the regulation, supervision, and oversight of FMIs.

See above

Responsibility D: Application of principles for FMIs **Central banks, market regulators, and other relevant authorities should adopt, where relevant, internationally accepted principles for FMIs and apply them consistently.**

Key considerations

1. Authorities should adopt the principles set out in this report.
2. Authorities should ensure that these principles, at a minimum, are applied to all systemically important payment systems, CSDs, SSSs, CCPs, and TRs.
3. Authorities should apply these principles consistently within and across jurisdictions, including across borders and similar types of FMIs.

See above

Responsibility E: Cooperation with other authorities **Central banks, market regulators, and other relevant authorities should cooperate with each other, both domestically and internationally, as appropriate, in promoting the safety and efficiency of FMIs.**

Key considerations

1. Authorities should cooperate with each other both domestically and internationally, to support more-efficient and more-effective regulation, supervision, and oversight of FMIs.
2. Authorities should use current and evolving best practices on international cooperative arrangements in relation to internationally active FMIs.
3. Relevant authorities should coordinate as needed to ensure timely access to trade data recorded in a TR.

See above