



Response to CPSS/IOSCO consultative report on a proposed assessment methodology for the oversight expectations applicable to critical service providers

Introduction

1. London Stock Exchange Group plc (LSEG) welcomes the opportunity to respond to the CPSS/IOSCO consultative report on a proposed assessment methodology for the oversight expectations applicable to critical service providers.
2. LSEG is a diversified international exchange Group, headquartered in London, with significant operations in Europe, North America and Asia. The Group operates a broad range of international equity, fixed income and derivatives markets as well as a range of Financial Markets Infrastructures (FMIs) including four Central Counterparties (CC&G and three within the LCH.Clearnet Group), a Central Securities Depository (Monte Titoli), and Unavista, an EMIR authorised Trade Repository.
3. In our response, we only deal with those aspects that are relevant to LSEG and LCH.Clearnet. The majority of issues we believe will be addressed more appropriately by the critical service providers themselves.
4. Our response stresses the need to provide a more specific definition of critical service providers and clarify how instances of non-cooperation of the critical service providers should be addressed particularly where there may not be an alternative service provider that the FMI could engage for these purposes. It also suggests that the assessment methodology is expanded to cover financial stability and people risk of the service provider. Finally, it provides some specific suggestions on QE1 'Risk identification and management'.
5. We acknowledge that this response may be published by CPSS/ IOSCO.

Definition of critical service provider

6. Annex F refers to a critical service provider as a third party that undertakes activities that are essential to the operations of the FMI. This is quite a broad definition which arguably could be applied to all service providers. We do not believe that this is the intention of the policy makers and would suggest that the definition of critical service provider is more specific along the lines described below.
7. We note that the paper envisages that the authority monitors compliance with the standards itself in a direct relationship with the service provider or that the FMI obtains assurances from the critical service provider that it complies with these standards. Where the FMI is responsible for checking compliance, the resources required to implement the suggested assessment methodology will be significant. It is therefore essential that the FMI is able to focus its effort on the service providers that will affect

Contacts:

Paola Fico, Borsa Italiana Regulation & Post-trading, +39 (0)272 426 285; paola.fico@borsaitaliana.it

Perrine Herrenschmidt, LCH.Clearnet, EU Public Affairs, +44 (0)20 7426 7246 ; perrine.herrenschmidt@lchclearnet.com



its ability to conduct its core functions and does not devote unnecessary resources on those providers that support services that are not essential or important to the operation of the FMI. A more specific definition will also help ensure a consistent approach across different jurisdictions.

8. We would suggest that the definition is limited to services that if not executed in an uninterrupted, secure and controlled manner could materially impact the clearing, settling or recording of payments, securities, derivatives or other financial transactions. Therefore, a service should be considered critical only where a failure in its performance would impair the FMI's ability to meet relevant regulatory requirements or the continued provision of core services. In addition, we would suggest that CPSS/IOSCO provides more specific guidelines regarding the types of activities that should be excluded from the assessment. Examples of services that should be excluded are personal security services; reception; mail sorting; cleaning of the premises; hardware maintenance services; individual computer software; payroll processing services; and consulting services (legal, IT, business analysis). Where a provider undertakes a mixture of critical and non-critical activities, the non-critical activities should be outside the scope of the assessment.
9. In addition, we would suggest that in the case of intra-group outsourcing of core activities, CPSS/IOSCO either clarifies that such arrangements are excluded or recommends a proportionate approach in recognition of the fact that these types of arrangement generally imply a lower level of risk. The level of control over the service provider is a key aspect for the FMI to consider when defining the outsourcing requirements. Therefore, while specific arrangements must be put in place to deal with intragroup outsourcing, there should be more flexibility as regards the level of detail of the assessment that FMIs should perform.

Responsibility for assessment of compliance

10. The paper notes that the assessment should be conducted by the critical service provider itself and compliance checked by the FMI or the authority. An FMI is likely to be only one client of the critical service provider and therefore its power to influence the supplier to spend time and effort in supplying the required information may be limited. Similarly, the FMI's authorities are unlikely to have jurisdiction over the critical service provider and their power to influence it would also be limited. We would therefore welcome clarification from CPSS/IOSCO that FMIs should not be precluded from using a critical service provider that has been non-cooperative, particularly where there may not be an alternative service provider that the FMI could engage for these purposes.
11. It is important that these principles do not inadvertently discourage outsourcing, which is generally recognised as enabling firms to achieve higher operational efficiency by

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Paola Fico, Borsa Italiana Regulation & Post-trading, +39 (0)272 426 285; paola.fico@borsaitaliana.it

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reducing costs through a specialisation of competences and additional organisational flexibility. The principles should seek to ensure FMIs and their relevant authorities ensure so far as they are able that the critical service providers meet the required standards.

Additional areas of consideration

12. One area of risk that can adversely affect the ability of a service provider to provide a suitable service to an FMI is its ongoing financial viability. We believe that this should be given more emphasis in the proposed assessment methodology. The only question that touches on this is how the supplier incorporates risk management into its strategic decision-making process, including assessment of general business risk and financial condition under QE1. We would also recommend CPSS/IOSCO considers adding some questions around the service provider's customer base to ensure there is no over dependence upon a single customer.
13. Another area of risk that could affect the FMI is people risk. Whether the service provider is dependent on key man risk and whether staff are screened prior to employment should be considered as part of the assessment methodology.
14. Finally, we would suggest including references to compliance with ISO International Standards, external assessment of provision of services or compliance with other best practice requirements. SAS 70 for example is an auditing standard designed to enable an independent auditor to evaluate and issue an opinion on a service organisation's controls.

OE1. Risk identification and management

15. The document envisages that the critical service provider assesses its risks and risk management framework on an 'ongoing basis' without setting a minimum standard. We believe that all risks should be assessed following any material change, either internal or external, to the organisation and at least annually. It is important to provide some metrics around this as an expectation of 'on-going' or continual assessment would be disproportionate.

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