BANKA SLOVENIJE
EUROSYSTEM

BANK OF SLOVENIA
Slovenska 35
15 05 Ljubljana
Slovenija
Tel.: +386 1 47 19 000
Telex: 31214 BS LJB SI
Fax: +386 1 25 15 516

Bank for International Settlements
Committee on Payment and Settlement Systems
CPSS secretariat (cpss@bis.org)

International Organization of Securities Commissions
Technical Committee of the International Organization of Securities Commissions
IOSCO secretariat (fmi@iosco.org).

Ref : 29.30-278/11-BP
Date : 15 July 2011

Subject: **Comments of Banka Slovenije on the Principles for financial market infrastructures, Consultative report**

Dear Sir or Madam,

Please find below comments of Banka Slovenije on the CPSS-IOSCO Principles for financial market infrastructures, Consultative report, March 2011.

Please note that the comments presented in this letter are provided from payment and settlements systems experts' point of view and should not be considered as official view of Banka Slovenije as a member of the Eurosystem.

In case of enquiries, please contact Mr Aljoša Šega (tel.: 00386 1 47 19 557, e-mail: aljosa.sega@bsi.si) or Mr Beno Ploj (tel.: 00386 1 47 19 575, e-mail: beno.ploj@bsi.si).

Yours faithfully,

P. Centrih

mag. Peter Centrih mag. Simon Anko
Payment and Settlement Systems

Individual comments

No.	Related to	Comment
1.	general	There is a mixed approach used to define the CPSS-IOSCO principles and key considerations. While some requirements are addressed to the institutions/entities (as operators of (payment and settlement) systems, CCPs or TRs), other focus on the substance (systems as arrangements between participants). We suggest that general guidance is provided on how to correctly apply the principles. See also next comment. In addition, it should be noted that one institution can act in different roles which all fit into the definition of FMI – as a CSD, a CCP, a TR or operator of an SSS. The principles should provide a clear basis for allocation of responsibilities if one institution e.g. operates an SSS and acts as CCP at the same time, in order to avoid any spill-over of risks between both functions. In such case, if clear allocation of risks and their management can not be ensured, a legal separation of different functions should be considered to contain risk.
2.	1.8-1.10	As defined in Annex H and also in paragraph 1.8, an FMI is "a multilateral system among participating financial institutions, including the operator of the system ..." When the draft CPSS-IOSCO principles are read with this definition in mind, it may be difficult to identify the addressee(s) of these principles and allocate the responsibility for compliance with them. First of all, an FMI is defined as a system and therefore lacks legal personality. Consequently, although requirements may be addressed to a system, they can only be fulfilled by its operator or (where applicable) its participants. According to the definition of an FMI, the system operator is (only) one of the participants in a system which, as an FMI, is addressed by the principles. While many principles or key considerations are aimed at addressing the arrangements and their participants as a whole (e.g. Principle 1 on legal basis or Principle 8 on settlement finality), others are clearly applicable to the operator of the system or of the infrastructure (e.g. key consideration 3 under Principle 4 on credit risk or Principle 15 on general business risk). The relevant responsibilities should be more clearly allocated. Alternatively, an appropriate explanation and clear guidance for users of the principles should be included in the introductory part of the document. According to paragraph 1.9., the "functional definition of an FMI includes five key types of FMIs: payment systems, CSDs, SSSs, CCPs, and TRs". However, some of these types of FMIs, especially CCPs and TRs, represent individual entities (or their functions) and, as such, are not "systems between participating financial institutions" as laid down in the definition of FMI. The definition of FMI should be amended / broadened accordingly. In addition, the wording that an FMI is "a system between participants" seems as an inaccurately broadened wording of the commonly used definition of a system as "an arrangement between participants".

		And in general, there should be greater consistency between the relevant definitions and within paragraphs 1.8. to 1.14.
3.	general	In general, the purpose of CPSS-IOSCO Principles should be to harmonise and strengthen all current market standards/principles for systemically important payment systems, CSDs, CCPs, SSSs and TRs in a single set of standards/principles. Therefore, it is unclear why such an approach was not fully followed for SSSs by excluding RSSS recommendations 2, 3, 4, 5, 6 and 12. This clearly creates the situation with two sets of world-wide recognised standards for SSSs. In our view, the fact that the above mentioned RSSS apply only to SSSs should not be seen as an obstacle for their incorporation in a common document since also in the draft CPSS-IOSCO Principles there are several principles with clearly limited applicability (e.g. principles 6 and 14 for CCPs, principle 24 for TRs). Only then would it be possible that the new principles completely replace all existing sets of standards.
4.	Principle 7	With respect to the establishment of a minimum liquidity requirement, we support the option "cover two" although there is clearly a trade-off between increased liquidity requirements and lower liquidity risk. However, the more emphasis is given on the prevention of materialisation of liquidity risk, the larger should be the incentives for effective risk management on the side of a single participant. Although each participant is obliged to contribute more collateral if a funding arrangement covers default of more then one participant with the largest net obligation, this consequently raises awareness that potentially defaulting participant contributes more (in absolute figures) own liquid assets in order to participate in coverage of its own default. This inevitably leads to situation where each participant has greater incentives for effective risk management.
5.	3.8.2	We do not question the requirement for a well reasoned legal opinion in order to "establish ~~at~~ the point **at** which finality takes place" (editorial comment). However, public authorities should request such legal opinion in the domestic context only in case of lack of clear legal basis. Also, it should be further clarified how this requirement would be applicable. Should the legal opinion only establish whether the system rules are compliant with relevant laws or should the opinion actually specify the point of finality? On the other hand, a well reasoned legal opinion should be necessary in a cross border context where legal regimes are not harmonised to a certain extent.
6.	3.9.2. vs. 3.9.3	It is stated in paragraph 3.9.2 that central bank assets have the lowest credit risk. We agree with this statement. However, we suggest either stating that such assets have no credit risk, or modifying the statement in paragraph 3.9.3 which states that the use of commercial bank money implies little or no credit or liquidity risk. Otherwise, it could be very hard to imagine that commercial bank money caries no risk, but the central bank money might.
7.	p. 58, paragraph 2	In the last sentence of the introductory paragraph under the title "Central securities depositories and exchange-of-value settlement systems" (page 58), the reference to "an exchange-of-settlement system" should be replaced by a reference to "an exchange-of-value settlement system".

8.	Principle 12/2	Key consideration 2 states that "settlement of two obligations can be achieved in several ways and varies by how trades or obligations are settled". While other key considerations in the draft CPSS-IOSCO principles are drafted in the form of requirements (e.g. "An FMI should ..."), this one is in a form of plain statement with no guidance for the user on what should be the required / desired arrangement in a particular FMI. We suggest redrafting this key consideration to better reflect the intent of its authors.
9.	3.12.3.	We suggest to amend description of DVP model 2 in order to state that a CSD can settle securities transfers on a gross basis throughout the day in exchange of simultaneous (real time or very shortly after) transfer of funds on a net basis. Current diction is misleading since it implies that there could be a larger time gap between cash and securities transfers, which would no longer be "a DVP".
10.	3.14.9.	The text in footnote 95 is only a repetition (mostly even literally) of the contents of the body text of paragraph 3.14.9. It should, therefore, be redrafted or deleted altogether.
11.	Principle 15	We are, in general, in favour of setting a requirement for an FMI to maintain sufficient equity capital or, more precisely, to hold sufficient liquid net assets. Holding a certain amount of capital in form of highly liquid assets allows for greater flexibility and better management of an FMI's general business risk. However, such requirements should not be treated in isolation from other (general) capital requirements for certain types of FMIs that exist in individual countries' legislation. Also, fixing minimum liquid net assets requirements to a certain number of months' expenses do not take into account different risk profiles and positions of individual FMIs and may result in considerable additional capital requirements or capital restructuring (to make it "high-quality and sufficiently liquid in order to be transformed into cash with little loss of value" (key considerations 3 and 4). The market regulator / overseer should have the authority for flexible interpretation of what is sufficient liquid equity in individual cases.
12.	3.17.13	Second sentence of paragraph 3.17.13. states that the secondary site should be located at an appropriate geographical distance. This statement is followed by footnote 110 which correctly stresses the importance of an FMI having as distinct a risk profile as possible between sites. As geographical distance is just one of the elements of distinction between risk profiles of different locations, we propose that a reference to different risk profiles is moved into body text, while keeping the detailed explanation in footnote 110, complemented by the reference to an appropriate geographical distance.
13.	Principle 17/5	Key consideration 5 requires an FMI's <u>critical IT systems</u> to resume operations within two hours following disruptive events. This text should be better reflected in the explanatory note, paragraph 3.17.13, where the relevant requirement appears stricter – it namely requires the (whole) FMI to resume (all) operations within two hours following disruptive events.

14.	Principle 20	According to the explanatory note (paragraph 3.20.1), a link is "a set of contractual and operational arrangements between two or more FMIs that connect the FMIs directly or through an intermediary". In our opinion, this definition includes also links between payment systems (both direct and indirect). Consequently, we believe that key considerations 1 and 2 of Principle 20 on links should be marked as applicable also to (links between) payment systems (see Annex D, p. 126).
15.	Principle 22/3	Key consideration 3 requires FMIs operating across borders to use or accommodate internationally accepted communication procedures and standards. This consideration seems to bring no added value since such requirements are already in place for all FMIs pursuant to key considerations 1 and 2. Even in part where key consideration 3 aims at interoperability/interconnectivity between FMIs, this is covered explicitly in key consideration 1 (text in brackets) and also in key consideration 2 (see e.g. last sentence of 3.22.3.).