London
Stock Exchange Group

LSEG Submission to CPSS – IOSCO on Principles for financial market infrastructures – Consultative Report

29 July 2011

Summary

1. Introduction

The London Stock Exchange Group (LSEG) welcomes the opportunity to submit its views on the CPSS – IOSCO Consultative Report on Principles for financial market infrastructures.

This submission represents the views and experience of London Stock Exchange plc, Borsa Italiana, CC&G and Monte Titoli; the London Stock Exchange Group is well qualified to provide comments on issues relating to principles for financial market infrastructures: the Group companies CC&G and Monte Titoli are authorised to operate as management companies of central counterparty services and central depositary and settlement system services.

The response is in two parts; the first part contains our general remarks on the CPSS-IOSCO consultation regarding the structure of the document, its possible enhancement as well as some overarching comments on the approach and on the aim of the Principles.

In the second part of the document we respond to individual Principles; common remarks – if any – are provided, followed by specific (CCP or CSD) comments.

2. General Remarks

The LSEG emphasises the importance of ensuring that the infrastructures supporting financial markets operate within a harmonised framework of principles. We believe that this is essential to enhance safety and efficiency in payment, clearing and settlement fields, reduce systemic risk and foster transparency and financial stability.

We also appreciate the effort to harmonise and reorganise the already existing three sets of standards (the CPSIPS, RSSS and RCCP) in a unified set of standards. On this aspect we believe that an additional effort should be pursued in order to include in the CPSS-IOSCO Principles also the 6 RSSS recommendations that remain in effect.

Consolidating the above mentioned three sets of standards in a single document that applies to all the financial market infrastructures has the clear aim of ensuring consistency of the framework which applies to FMIs act and of avoiding duplication. However, although a strong effort to provide functional definition is evident, a single document for all FMIs is probably not the clearest approach.

Each type of FMI covered by the CPSS-IOSCO Principles has particular characteristics and it is, in some cases, not easy to interpret which statement applies to which FMI (e.g. 3.5.7; 3.7.6; 3.7.16; 3.8.3-3.8.6; 3.10.4 and principle 12 do all actually apply to CCPs?).

To improve clarity the current document structure could borrow from Principle 20, whose structure is based on a general part followed by

specific parts applicable to each type of FMI (CSDs, CCPs, TRs), save for those Principles such as Principle (Legal Basis) which could continue to apply to all FMIs..

Moreover the CPSS-IOSCO Principles involve a large overhaul of the whole view on market infrastructures and this is occurring at the same time as other regulatory measures are under discussion, both at EU level (EMIR Regulation; CSD Legislation; Basel III Regime) and US level (Dodd-Frank Act). As an EU FMI, we strongly hope that existing areas of inconsistency between CPSS-IOSCO and the EMIR Regulation will be resolved and that CPSS-IOSCO Principles will be reflected in the forthcoming discussions regarding the draft CSD Legislation.

At the same time we emphasize the heavy regulatory and compliance burden to which FMIs are subject and the organizational efforts required to react to the changing regulatory framework. This has high impacts in particular on CCPs considering that only CPSS-IOSCO compliant CCPs are eligible for the Basel III "*Qualifying Status*" and the tight deadline for the entry into force of Basel III (January 1st, 2013).

Another factor to consider is the current basis for supervision and oversight in Europe, which is based on the ESCB-CESR Recommendations. We strongly recommend that a single set of principles applies in the European Economic Area in order to avoid both the duplication of efforts and possible inconsistencies or conflicting requirements and interpretations.

2.1 General Remarks on the document structure

Regarding the document structure, we confirm our appreciation for the effort performed to merge the previous different existing sets of standards/recommendations into a single document collating the applicable Principles. Much work has been done but some areas for improvement remain. In particular: some concepts are expressed more than once (e.g. 99% margin coverage is mentioned 9 times[1] in the document) and there is an apparent duplication/overlap of concepts: in particular Principle 3 appears to synthesize concepts detailed in the following Principles 4-6.

We also are uncertain on the status of Annexes. In particular we are seeking clarification as to whether Annex E is part of principles or pure guidance and if a CCP has to assess compliance also with it in order to be compliant with CPSS-IOSCO Principles (and in final instance being recognized as "qualified CCP" for the Basel III regime).

An additional issue is related to the unavailability of an assessment methodology. We highlight that to provide a common methodology is

[1] Principle 4, Key Consideration 4; Principle 4, Key Consideration 5; Paragraph 3.4.9 (twice); Paragraph 3.4.11; Principle 6, Key Consideration 3; Paragraph 3.6.6; Paragraph 3.6.12; Paragraph 3.6.14.

essential to perform a consistent gap analysis and assessment by the FMIs covered by the Principles. To this extent we anticipate that the assessment methodology will also be subject to consultation together with the next version of the CPSS-IOSCO Principles.

On this specific topic we strongly believe that separate assessment methodologies for each type of market infrastructures would be extremely beneficial as opposed to a single assessment methodology for all FMIs. Such an approach will produce tightly focused assessment approaches which will better address specific issues relevant to each type of FMI. By reducing the need to rely on interpretation, more uniform application and assessment across different jurisdictions and assessors will be ensured.

2.2 General Remarks from CCP perspective

As mentioned above CPSS-IOSCO Principles present a number of interconnections with EMIR, DFA and Basel III.

We believe it is important to manage these interconnections avoiding contradictory statements in order to allow a clear understanding and compliance with the principles/rules by the CCPs (e.g. Risk Committee composition/scope, etc). Moreover, given the different jurisdictions for which the CPSS-IOSCO Principles and EMIR are applicable, we want to highlight the risk of regulatory arbitrage against CCPs located inside the EU in favour of CCPs located outside the EU whenever EMIR would adopt stricter requirements than CPSS-IOSCO Principles (e.g. EMIR foreseeing coverage of the two most exposed members; CPSS-IOSCO foreseeing coverage of the most exposed member).

An alignment of CPSS-IOSCO Principles and EMIR and other relevant pieces of legislations such as DFA is necessary to allow fair competition between CCPs, regardless of their country of incorporation.

CPSS-IOSCO Principles also introduce a “duty of care” of the FMIs towards the participants’ customers[2]. We believe that this should be out of scope of the Principles as it is not appropriate that a FMI is obliged to assume responsibilities for customers with whom they have no legal relationship.

In particular, with reference to CCPs, they are generally considered to have a legal relationship only with their participants (i.e. those entities that fulfil predefined participation requirements and are scrutinised by CCPs).

Direct participants have the legal responsibility toward the central counterparty for the entities on whose behalf they act and are also responsible in the case of failure of their customers. It is up to CCPs’ direct participants to assess and manage the risk posed by their respective

[2] Ref. Principle 3, Key Consideration 2; Paragraphs 3.3.4, 3.3.5; 3.19.2; 3.19.3.

customers, towards which they are the only ones who have legal responsibilities.

In common with other European CCPs, we strongly believe that CCPs should not be obliged to accept a direct risk on the clearing members' customers nor any extensive duty of care for these customers. Nonetheless we see some possible benefits in the introduction of more granular account structures and we believe that direct participants should be allowed to maintain segregated accounts for individual clients, provided that the legal responsibility towards the FMI remains solely in the relation with the direct participant.

Last but not least, CC&G strongly supports the comments provided by EACH on the CPSS-IOSCO principles insofar as compatible with the comments provided in this document, having actively contributed to drafting the contribution provided by the European Association of CCPs.

2.3 General Remarks from CSD/SSS perspective

From the CSD/SSS perspective, as well as for CCPs, a number of interconnections exist between the CPSS-IOSCO Principles and the forthcoming CSD Legislation; it is important to manage these interconnections avoiding contradictory statements, to allow a clear understanding and compliance, and avoiding the risk of regulatory arbitrage.

Moreover the Principles have a strong insight on credit risk evaluation, monitoring participants' exposures, risk analysis and "Know Your Customer" rules[3]. In our understanding CSD/SSS are required to comply with these Principles only when performing banking activities or banking type activities. We believe that to avoid any misunderstanding this should be clearly specified.

Monte Titoli also supports the comments provided by ECSDA on the CPSS-IOSCO principles insofar as compatible with the comments provided in this document, having actively contributed to drafting the contribution provided by the European Association of CSDs.

3. Detailed Remarks to specific principles

Principle 1: Legal Basis

Common Remarks

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

[3] Ref. Principles 4, 5, 7; 3.18.5 and Principle 20, Key Consideration 3.

Considering that FMIs regulation is contained in the law and authorities' regulations, which are clear, transparent and enforceable by definition, and that FMIs' rules are based on this regulatory framework and approved by relevant authorities, we believe that the certainty of the legal basis of an FMI is assessed by the competent authority also during this approval/recognition phase.

Regarding cross border activities, we are supportive of the role of legal opinions in articulating the legal basis. However it is our opinion that this requirement should not apply within the EU/EEA due to the harmonization of important aspects of the legal framework that have been and are being harmonised.

Moreover, this requirement should take into account that for non EU/EEA entities their participation to EU/EEA FMI services is subordinated to local authorities' authorization, based on substantial equivalence of the legal framework evaluation. For this reason there is a possible overlapping between the legal opinions requested by CPSS-IOSCO principle and the authorization released by the authority.

Furthermore it would be up to the participant to demonstrate that there are no legal obstacles or conflicts of law, arising from its regulatory framework, that prevent them from complying with the requirements and the constraints imposed by the legal framework applicable to the FMI with which they intend to participate.

Principle 2: Governance

Common Remarks

The Principle (with particular reference to par.3.2.9) requests policies for the functioning of the Board and also mentions the committees the FMI's Board is expected to have.

It is quite common that the organisation of such committees is managed at the Group level within a company, without setting up the similar committees in every single company within the Group.

The same holds true for the policies adopted by the Group and applied where relevant by all companies in the Group.

It is our understanding that this kind of governance structure is in line with the CPSS-IOSCO requirements and therefore sufficient to demonstrate compliance with the Principle.

CC&G

We broadly support the proposed drafting of Principle 2.

More specifically, we appreciate and deem viable the Risk Committee composition outlined in paragraph 3.2.12 as "chaired by a sufficiently

knowledgeable independent board member and consist of a majority of board members that are independent of management".

We would like to highlight that this requirement is in sharp contrast with the provision of the EMIR drafts, which in article 26 require that CCPs must have a "*Risk Committee composed of representatives of its clearing members and independent members of the Board, chaired by an independent member of the Board, allowing clients to participate or be appropriately represented*".

Therefore these different approaches would result in the obligation for European CCPs to establish two different Risk Committees with different mandates and compositions and working rules.

In our opinion there should be better coordination between regulatory bodies to ensure that FMIs are subject to consistent requirements and in this specific case to avoid the double obligation on CCPs to have two different Risk Committees, with different participants and with different functions and possibly different approaches and risk appetites which may eventually end up jeopardizing the transparency and quality of risk management decisions.

We strongly believe that the possible conflict of interest arising from the client's interests that may be different from those of the CCP should not be underestimated and therefore we favour board structures as the one proposed by CPSS-IOSCO that minimises the possibility of conflict of interests and that has a clear allocation of risk taking decisions.

Principle 3: Risk Framework

Common Remarks

One of our main areas of concern is the possible introduction of forms of direct responsibilities or other "duties of care" for FMIs towards entities which are not Direct Participants.

Our concerns arise from the statement in Key Consideration 2 (and further confirmed under par. 3.3.4 and 3.3.5.of this principle) whereby "*An FMI should provide incentives and, where relevant, the capacity to participants and their customers to manage and contain their risks.*"

We appreciate the upsides of FMIs providing incentives to its participants to manage and contain their risks, and we support the principle that FMIs should put appropriate incentives in place. However we believe that the most effective incentives that the FMI can provide, consist of policies aimed at monitoring *its own participants* to prevent behaviours that are incompatible with the well-functioning of the system. Appropriate sanctions providing for suspension from the system should complement those policies.

We also see some possible benefits in the introduction of more granular account structures and we believe that a CCP should offer a variety of clearing models with different levels of segregation to suit the needs of their clearing members and their clients.

However, it is our opinion that it is not the role of the CCP to "require" this level of segregation of its clearing members and that the provisions, as currently drafted, regarding the participants' customers may be excessive, as they go beyond the role and the powers of FMIs and exceed their abilities and competences. Specifically when FMIs are required to provide their participants and the customers of their participants with the "capacity" to manage their risks.

We are concerned that the word "capacity" might be interpreted as meaning not only reports containing information about positions, exposures and margin requirements, but also as providing tools, systems or even resources to clients of direct participants.

In our view this not only puts an inappropriately high a burden on FMIs but it also does not give adequate consideration to the responsibility of clearing members and their clients to implement and run their own risk management.

This would lay a burden on FMIs which they cannot reasonably be expected to support and would make them liable for the risk management which should be performed by the direct members. The LSEG is of the opinion that the words "*the capacity to participants (...) to manage and contain their risks*" should be replaced by: "*the information (as specified in the rules and procedures of the FMI) to participants (...) to manage and contain their risks*."

Another difficulty emerges if the client's client level is considered: in indirect holding systems, in fact, FMI operators do not know the customers that their own participants are acting for. In such cases it is unclear how incentives and capacity can be provided to them.

In addition, we also note that by extending to the customers of participants the requirement on FMIs to provide incentives and the capacity for appropriate risk management, seems to imply the existence of some sort of legal relationship (e.g. "a duty of care") between the FMIs and their participants' customers.

Consequently we propose that "*and their customers*" is removed from Key Consideration 2 and from paragraph 3.3.4.

As a final comment on this principle we would like to point out that the sentence contained in paragraph 3.3.2 (and in Key Consideration 3) "*an FMI should first identify the range of risks that arise within the FMI and the risks it directly bears from or poses to its participants, their customers, and other entities*" is clearly overstretching the responsibilities of the FMI, we propose to delete "*poses*".

Principle 4: Credit Risk

CC&G

We agree with the contents of Principle 4. However CC&G would like to highlight that the sentence "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" contained in the Key Consideration 7 and the related topics stated in paragraph 3.4.16 may be probably better placed under Principle 7 as it is relating to liquidity risk issues.

Regarding the number of defaults to be covered, we advocate the approach that considers the default of the two most exposed participants, independent of asset class, provided this is applied consistently world-wide in regulation in order to avoid (a) improper regulatory advantages in favour of non-EEA geographical areas and (b) the possibility that some FMIs would end up needing to comply simultaneously with different regulations following different philosophical approaches.

Monte Titoli

The overall impression is that the contents of the Principle specifically cover cases in which the CSD/SSS provides credit facilities to its participants or takes principal risk in the settlement process. Otherwise, the provisions are hardly applicable.

We would like to propose that such distinction clearly emerges from the final version of the Principle so that the contents are more focused on the specific activity of the addressee.

Principle 5: Collateral

CC&G

We note that the wording of paragraph 3.5.2 that states that a CCP "*should avoid wrong-way risk by not accepting collateral that would likely lose value in the event that the participant posting collateral default*" is too general and needs to be tighter.

In general CC&G agrees with the need to identify and manage the wrong-way risk on collateral but it appears not viable in some cases. For example, in the case of default of a participant that is the major bank of a country, the government bonds issued by that country would lose value. So, according to this statement, these bonds should not be accepted as collateral by the CCP. The same example works in the case of currency of that country posted as cash collateral.

In our opinion a CCP should be not prohibited from accepting collateral with a likely wrong-way risk, but it should be established that the CCP

monitors the wrong-way risk on collateral and to implement the necessary procedures to manage it. So CC&G proposes to replace the words "*not accepting*" by "*monitoring*".

CC&G would also like to have clarification regarding the applicability of paragraph 3.5.7 to CCPs in case it offers a collateral management service or – as we believe – it is applicable only to CSDs.

On a broader level, and as mentioned in paragraph 2 (General Remarks) we believe that also in this instance, the clarity of the document would strongly benefit if the structure used for Principle 20 were to be more widely used and applied to other principles.

Monte Titoli

It is our understanding that this Principle applies only to entities providing collateral to their participants not to those CSDs/SSSs simply operating a collateral management system without directly providing collateral to their participants. However, par. 3.5.7 seems to cover also the latter because it lists the requirements that the information system used to monitor and manage collateral arrangements must have. If this is the CPSS-IOSCO intention, we understand that the "*sufficient resources*" quoted in the paragraph only applies for those CSDs that provide credit and banking type services.

Principle 7: Liquidity Risk

CC&G

The last sentence of the Key Consideration 3 "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" is apparently limiting CCPs liquidity needs to margin payouts, without considering settlement. CC&G would like clarification as to whether this is the intention.

In paragraph 3.7.8 the text refers again to "*same-day close out or hedging*" of defaulters' positions. This is apparently more stringent than EMIR – which does not set specific terms – and potentially in contradiction with the forthcoming Crisis Management legislation, where it is possible that rules will be introduced allowing the effective freezing of financial markets contracts. Such suspension of close out netting may frustrate the operation of any default rules and custom and practice in various financial markets. This must be avoided.

Regarding the number of defaults to be covered, the same considerations expressed under principle 4 apply here for principle 7 above.

In the context of central bank services (3.7.11) we would make the following remarks;

- The term “central bank credit” could refer to a number of different facilities:
    - an account with a central bank where a CCP can deposit assets;
    - intra-day credit to smooth the timing between incoming and outgoing cash flows during the course of a trading day;
    - overnight liquidity, where a CCP would rely on a central bank to cover a late payment running over more than a single day;
    - bailout support during a crisis (lender of last resort).

In this context of the first three of these (lender of last resort does not really constitute central bank liquidity) we believe that Principle 7 should not require CCPs to hold banking licences as the route to get access to this central bank liquidity. While we think it is important for CCPs to have central bank oversight and access to intra day funding lines from central banks, a banking licence need not be required for these “restricted banking activities”.

Monte Titoli

The principle refers to the liquidity risks raised from the FMI’s participants, recommending that appropriate measuring and monitoring tools are adopted.

We would like to note that entities acting as participants to a CSD/SSS are mainly banks that have been duly authorized to perform their activities by the competent authorities. The latter are responsible for setting the requirements to be granted the banking license and for ensuring the soundness of economic resources. CSDs/SSSs rely on the authorities’ assessment for admission to their services. From the responsibilities given to the CSD/SSS it is evident that the role of the authorities has not been duly considered.

Principle 8: Settlement Finality

Common Remarks

We notice that the concept of finality embraced by the Principle mainly refers to the “conclusion” of the transaction. This appears from the definition of final settlement provided for in 3.8.1 “*Final settlement is defined as the **irrevocable and unconditional transfer** of an asset or financial instrument or the **discharge of an obligation** …”*. Within the European legal framework a specific legislative text (Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement

finality in payment and securities settlement systems, called the Settlement Finality Directive - SFD) addresses:

- legal enforceability
- binding nature towards third parties in the event of insolvency proceedings against a participant
- irrevocability.

All of the former are recognized to **transfer orders** i.e. to instructions made by participants in the system. These principles have been in force in European Member States since the implementation of the SFD in the domestic legal framework. For this reason we would like to be assured that Principle 8 is fully consistent with the EU legal framework.

We also think that the Principle does not take into consideration the role that in some markets is played by CCPs in connection to the settlement of guaranteed trades. In the event these trades cannot be settled on ISD, buy-ins and sell-outs are activated by the CCPs without the direct involvement of the CSDs. For this reason we recommend that the role of CCPs is fully and appropriately recognized.

Finally, the provision of a legal opinion is recommended by par. 3.8.2 to clearly establish the point at which finality takes place. We are aware of the complexity of the issue and supportive of the role that a legal opinion may have in legal framework that do not provide certainty on finality. However, we would like to stress that this must not be considered a requirement for EU/EEA countries due to the wide the application of the SFD principles that both:

- harmonize the concept of finality
- give to the systems the responsibility to determine the moment at which finality takes place.

Principle 11: Central Securities Depositories

Monte Titoli

The principle presents the concept of legal separation between the custody and settlement activities and the other activities performed by the CSD as a possible risk mitigation tool. It is our opinion that such separation is not necessary and would make the provision of services aimed at facilitating settlement less efficient.

We think that, when a CSD is duly authorized by relevant authorities, it should be able to perform both core and ancillary services without any further requirement. This includes the provision of ancillary banking services related to settlement, notary and central safekeeping functions and to corporate actions, which are important in ensuring the settlement

process and which we do not consider to be high risk activities. There should be no requirement to hold a separate banking licence in order to provide these services..

Principle 12: Exchange-of-value settlement systems

CC&G

According to the table in Annex D this principle is applicable to CCPs. However, we do not observe any paragraph under this Principle which we consider to be relevant for CCPs. Therefore we request for more clarification in the text as to why and to which extent this Principle could be applicable to CCPs.

Principle 13: Default Management

CC&G

CC&G notes that paragraph 3.13.2 (c) – that foresees "*changes to normal settlement practices*" – is apparently contradicting paragraph 3.13.1 (a) – that aims at "*ensuring timely completion of settlement even in extreme but plausible market conditions*" – and 3.8.3. – that states that "*an FMI that does not provide final settlement on the value date would not satisfy this principle…*".

Building up on our previous comments, CC&G suggests that the viability of close-out netting should be explicitly stated.

We believe that the sentences (in paragraph 3.13.3): "The rules of the FMI should specify the order in which different types of resources will be used" and "Typically an FMI should first use assets posted by the defaulting participant, such as collateral and margins (sic)…" have space for two improvements. The first one is by removing the word "margins" as a CCP would use also other assets (e.g. contributions to default funds) provided by the defaulter. In addition, we feel that it is important to clarify that this order in using assets should apply exclusively to loss allocation and not to liquidity needs.

Principle 14: Segregation and Portability

CC&G

The statement in paragraph 3.14.1 "Segregation also protects a customer's collateral from becoming unavailable or permanently lost as a result of a participant's insolvency" – if applied to CCPs – suggests that customers' collateral is posted at the CCP itself. In practice the collateral deposited at the CCP by the clearing member is not necessarily the same collateral which has been deposited by the customer at the clearing member.

It is often the case that the clearing member deposits with the CCP different collateral representing the same or similar value (depending on the specific margin requirement) as the collateral deposited by the customer with the clearing member.

As a consequence the CCP will not be able to transfer the customer's collateral to another clearing member but might be able to transfer collateral deposited by the clearing member in respect of customer positions.

The same comment applies also to paragraph 3.14.6 where it also refers to a customer's asset.

CC&G believes that the Principles should clearly state that the collateral referred to are "*assets deposited by the Clearing Member for the account of the client*".

The sentence "The CCP should maintain collateral supporting customer positions in an omnibus account or in individual accounts at the CCP or its custodian" in paragraph 3.14.10 hints at having end customers accounts at the CSD. CC&G points out that an adequate level of segregation can be provided by CCPs without need of having individual accounts at the custodian level.

The sentence "In addition, assets held by the participant should be limited to any excess collateral posted by the customer beyond that which is required by the CCP to cover its exposures" contained in paragraph 3.14.10 appears to be a requirement for participants in relation to their clients rather than a requirement for FMIs. Accordingly CC&G would propose to delete this sentence.

Principle 15: General Business Risk

Common Remarks

Regarding the capital requirement for CCPs, we note a discrepancy between CPPS-IOSCO Principles and EMIR draft regulation. In fact the former sets a variable capital requirement, whereas the latter sets a fixed capital requirement plus the requirement to be able to ensure the orderly winding down of the company. As said before, CC&G advocates for consistent approaches in various regulations.

Along a similar line, we also comments that the issue of capital requirements is under discussion within the European Commission also for CSDs, in preparatory works of a future legislative instrument (CSD Directive) specifically addressed to CSDs. It is context it is important that consistency is granted.

Moreover we believe that providing for a fixed capital requirement is sufficient to ensure a proper organizational set up of an FMI.

In fact FMIs are regulated because they perform a systemically relevant activity and to this extent they are requested to satisfy a number of requirements, including to have an adequate amount of capital.

Vice versa once FMIs cease to perform such systemically relevant activity, there is no longer a public interest in ensuring their solvency and for this in our understanding there is no reason to request them to satisfy any type of variable capital requirement or having resources for winding down the company.

Principle 17: Operational Risk

Common Remarks

We note that Paragraph 3.17.4 states: "an FMI should comply with, or, depending on the FMI's importance and level of interconnectedness, exceed the relevant industry's best practices." We understand that an FMI should aim to comply with best practices, but we believe that a requirement to exceed best practices is a contradiction in terms.

Principle 18: Access

Common Remarks

In paragraph 3.18.2 the statement reads "*An FMI's participation requirements should therefore encourage broad access, including access by participants, other market infrastructures, and where relevant service providers, in all relevant jurisdictions, based on reasonable risk-related participation requirements*".

We propose an amendment in the wording of the paragraph replacing "*encourage*" with "*allow*" in order to make it line with Key Consideration 1 ("an *FMI should allow for fair and open access*...") to consistently reflect the obligations of the FMIs in the field of access.

In addition, we also note that the issue of access is currently under scrutiny by the European Commission within the future legislation on CCPs and CSDs. We recommend that efforts are made to ensure consistency between these legislative developments and the requirements of this Principle.

Principle 19: Tiered Participation Arrangements

Common Remarks

LSEG notes that the broad principle contained in paragraph 3.19.1 encouraging "*FMIs to identify, understand, and manage their risks arising from tiered participation arrangements*", is appropriately counterbalanced by the recognition "*that the ability of a particular FMI to identify, understand and manage all such risks is likely to be limited*."

The limited capacity FMIs have in managing risks arising at clients level is repeatedly recognised throughout the explanatory notes when wording is used such as "*to the extent practicable*", "*to the extent possible*", "*there are limits to the extent to which an FMI can...*", "*an FMI may face legal or practical constraints*" etc, and we believe that all these limitations raise significant uncertainties doubt regarding the possibility of an effective assessment of FMIs against this principle.

We believe that the explanatory notes are identifying existing constraints and limitations that FMIs are actually facing, as a matter of fact most FMIs act on a principal-to-principal basis; thereby excluding any legal relationship and obligation towards the clients of their clearing participants and we have serious doubts that FMIs may actually enforce any risk mitigation actions against clients. We strongly believe that direct participants are responsible for the appropriate management of their clients.

We also note that paragraphs 3.19.5 and 3.19.6 contain supervisory tasks that are beyond the scope of FMIs. The only institution having a global overview of the exposures of the clients and their concentrations of risk is the home country regulator of this client.

Accordingly we would therefore propose to clarify that FMIs do not have supervisory duties on what participants do with their clients.

CC&G

LSEG believes that the statement in paragraph 3.19.4: "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" should be articulated in such a way to reflect the role and responsibilities of direct participants. Most CCPs do not have any legal relationship with the clients of its clearing members and hence the need for the clearing members to have the responsibility for managing this risk.

Monte Titoli

With particular reference to CSDs/SSSs, in indirect holding systems, obligation of activities of identification and of monitoring of the indirect participants would be very difficult to fulfil due to the impossibility of those systems to know their participants' client.

Moreover, it seems that the Principle does not take in consideration that participants, due to their direct relationship with the system, are deemed responsible towards the system itself also for the activities they perform on behalf of their own clients.

Principle 20: FMI Links

Common Remarks

We particularly appreciate the clarity of the structure of this Principle (Introduction, CSD, CCP, TR) and we encourage CPSS-IOSCO to apply where possible the same structure to other principle.

CC&G

CC&G notes in paragraph 3.20.11 an apparent contradiction between the following statements: "*Exposures faced by one CCP from its linked CCPs should be monitored and managed to the same confidence level as exposures from a CCP's participants*" and "*If a CCP provides initial margin to another CCP under a link, that margin should be at least equal to that which would be given for the same position by a participant that is not a CCP*".

If anything, CCPs have a less risky profile than participants, and this is also recognized by the Basel III Regime.

So CC&G would propose to replace in the first sentence the wording "*to the same confidence level*" by "*to a confidence level not higher than*" and to replace in the second sentence the wording "*at least equal*" by "*no higher than*".

The statement in paragraph 3.20.13 "*Another source of risk may emerge if a linked arrangement treats the linked CCP differently from other participants, such as setting less strenuous participation requirements for the linked CCP than for other participants*" seems to neglect that CCPs are different companies than members firms and that some membership requirements may simply be inapplicable.

Of course CC&G agrees about the fact that CCPs are different entities and have a very different risk profile than member firms and different participation requirements are in some instances justifiable. We believe that the correct requirements are those that capture appropriately the specific risk profile of the linked entity. therefore certain "*less strenuous*" membership requirement may just be "*more appropriate*" as it correctly indicated in 3.20.15 [cf. also paragraph 3.20.16].

So CCG propose is to replace the wording "*differently from other participants, such as setting less strenuous participation requirements for the linked CCP than for other participants*" to "*without fully evaluating the specific risk profile of the linked CCP*".

CC&G also notes that the statement in paragraph 3.20.14 "Further*, they should maintain risk-management arrangements which may involve a separate default fund to cover risk from a link*" can be dangerously misleading as it may be read as an additional layer of mutuality resources (whose unspecified contributors would be exposed to losses in case of

default of the linked CCP) and in addition the wording "*default fund*" hints in a precise direction.

CC&G suggests that the words "*specific additional resources*" maybe is more appropriate than "*separate default fund*". Alternatively the whole last sentence can be cancelled.

The sentence in paragraph 3.20.16 "The CCP that provides an account to another linked CCP may therefore need to hold additional financial resources to protect itself against the default of the linked CCP" does not appear to be correct. As indicated a few lines above "…the CCP that maintains an account for another CCP would typically require the other CCP to provide margin…" therefore is the acceding CCP that has un-collateralized exposure vis-à-vis the accessed CCP (i.e. the CCP that provides/maintain an account to/for another CCP). In general the whole paragraph has space for improvement in terms of clarity.

Principle 23: Disclosure of key rules and procedures

Common Remarks

It is recommended that "*other information*" are provided by the FMI to further enhance the understanding of its activities and operations (par. 3.23.6). However, no indication is given about the language required for the provision of such information. We would like to propose that, as minimum requirement, the local language(s) and a commonly used business language is used.

CC&G

Disclosure to participants of details of stress tests as stated in paragraph 3.23.6: "information that should be disclosed to participants, but typically not to the public, include key highlights of its business continuity arrangements, as well as details of stress tests and other data to help participants understand and manage their potential financial risks from participation in the FMI" does not appear appropriate for CC&G.

In our opinion it should rather specify that a CCP should provide information regarding the stress test methodology and the scenarios applied, but it cannot disclose any detailed result of stress tests due to reason of confidentiality and opportunity.

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