



31 July 2012

Publication of a consultative report on the recovery and resolution of financial market infrastructures

CPSS and IOSCO are publishing for public comment a consultative report on the *Recovery and resolution of financial market infrastructures*. CPSS and IOSCO request comments on the report by 28 September 2012. These comments will be taken into account by CPSS and IOSCO in the publication of further work later in 2012.

Financial market infrastructures (FMIs) play an essential role in the global financial system. The disorderly failure of an FMI can lead to severe systemic disruption if it causes markets to cease to operate effectively. Accordingly, all types of FMIs should generally be subject to regimes and strategies for recovery and resolution.

Consistent with this approach, the CPSS-IOSCO *Principles for financial market infrastructures (Principles)*, published in April 2012, require that FMIs have effective strategies, rules and procedures to enable them to recover from financial stresses. The Financial Stability Board's *Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes)* further require that jurisdictions establish resolution regimes to allow for the resolution of a financial institution where recovery is no longer feasible. An effective regime must enable resolution without causing systemic disruption or exposing the taxpayer to loss. For FMIs, this means applying particular emphasis on ensuring that the relevant authorities are given powers to maintain an FMI's critical services if they consider this necessary to maintain stability.

(i) Objectives of the report

The main purpose of the report is to outline the issues that should be taken into account for different types of FMIs when putting in place effective recovery plans and resolution regimes in accordance with the *Principles* and the *Key Attributes*.

As part of this exercise, the report also sets out how the specific key attributes apply to FMIs, identifying where relevant those elements that do not apply or require specific interpretation in some or all types of FMIs.

Finally, the report seeks views on a number of technical issues related to the way in which recovery and resolution measures should be applied. For ease of reference, these are listed at the end of this document.

(ii) Structure of the report

The report describes: (1) the relationship and continuity between the *Key Attributes* and the *Principles*; (2) recovery and resolution approaches for different types of FMI; (3) important interpretations of the *Key Attributes* when applied to FMIs; and (4) cooperation and

coordination among relevant authorities. The report is further supplemented by an annex which provides CPSS-IOSCO's interpretation of each key attribute as it relates to FMIs.

(iii) Conclusions of the report

The report concludes the following:

1. It is vital that very robust arrangements exist for the recovery of FMIs and, if that fails, for their resolution.
2. The *Principles* set out a framework for FMIs to have rules and policies for recovery in the event of distress.
3. Regulators will need to ensure that those rules and policies are put in place. The provisions for cooperation and coordination among authorities in Responsibility E of the *Principles* will help that.
4. In the event of recovery failing, the *Key Attributes* provide a framework for resolution of FMIs under a statutory resolution regime. The methodology for assessing compliance with the *Key Attributes*, currently being prepared by the Financial Stability Board, will need to contain FMI-specific elements.

(iv) Request for comments on the report

CPSS and IOSCO seek general comment on the consultative report including views on whether there are additional issues or circumstances that are not included in the report which may need to be taken into account in developing recovery and resolution strategies for FMIs.

In particular, the report poses the following questions for which views are sought (the questions are listed here in the order in which they appear in the report):

- In what circumstances and for what types of FMI can a statutory management, administration or conservatorship offer an appropriate process within which to ensure a continuity of critical services?
- Are there powers beyond those of a standard insolvency practitioner that a statutory manager, administrator or conservator would require in these circumstances?
- Is tear-up an appropriate loss allocation arrangement prior to resolution of a CCP? If so, in what circumstances?
- To what extent should the possibility of a tear-up in recovery be articulated in ex ante rules?
- Should there be a limit to the number of contracts that are eligible for tear-up?
- How should the appropriate haircuts be determined?
- What qualitative or quantitative indicators of non-viability should be used in determining the trigger for resolution for different types of FMI?
- What loss allocation methods must be available to a resolution authority, and for which types of FMI? Could or should these resolution powers include tear-up, cash calls or a mandatory replenishment of default fund contributions by an FMI's direct participants? Does it make a difference if the losses are from a defaulting member or are made up of other losses (eg losses in investments made by the FMI)? In what circumstances, and by what methods, should losses be passed on beyond the direct participants – eg to the clients or FMI shareholders – in resolution?

- What, if any, special considerations or methods should be applied when allocating losses whose maximum value cannot be capped (eg when allocating potential losses that might arise from open and uncapped positions at a CCP)?
- How should equity in FMIs be treated in resolution scenarios: should it be written down in all circumstances?
- Are there circumstances in which loss allocation in resolution should result in a different distribution of losses to losses borne in insolvency? Does it make a difference if the losses stem from a defaulting member or are made up of other losses (eg losses in investments made by the FMI or resulting from operational risks)?
- Should an FMI's rules for addressing uncovered losses be taken into account when calculating whether creditors are no worse off in resolution than in liquidation?
- Are there any circumstances in which the ability to exercise termination rights as a result of the use of resolution powers should outweigh the objective of ensuring continuity?
- Are there any circumstances in which a temporary stay on exercising termination rights should apply for any event of default and not just where triggered by the resolution measures?
- Are there any circumstances in which a moratorium with a suspension of payments to unsecured creditors may be appropriate when resolving an FMI? Should this be limited to certain types of FMI and/or certain types of payment?
- If so, should resolution authorities retain the discretion to apply a moratorium and, if so, what restrictions (if any) on its use would be appropriate (eg scope, duration or purpose)?
- Should the bail-in tool be available to collateral, margin (including initial margin) and other sources of funds if they would bear losses in insolvency?
- In what circumstances and for what types of FMI should wider loss recovery arrangements exist beyond the FMI's own rules and the resolution powers of the resolution authority?
- In conducting a resolvability assessment of an FMI, what factors should authorities pay particular attention to?

In addition, is the summary of the application of the *Key Attributes* to FMIs provided in the annex sufficiently detailed to support the development of recovery and resolution regimes for FMIs? Are there specific areas where more detail could be provided? If so, which areas and what additional detail should be provided? Are any of the key attributes not applicable to a particular type of FMI? If so, which key attribute(s) and why not?