

Svein Andresen
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☰ 1 PLUS i GmbH response to Financial Stability Board consultation on Guidance on Continuity of Access to Financial Market Infrastructures (“FMIs”) for a Firm in Resolution

Dear Mr. Andresen,

1 PLUS i welcomes the opportunity to comment on the consultative document regarding Financial Market Infrastructure. Founded in 2003, 1 PLUS i provides advisory services in the key fields regulatory laws, risk management, trade systems, financial products, and financial mathematics.

Particularly in regulatory laws, 1 PLUS i is specialized on all matters concerning the Bank Recovery and Resolution Directive (BRRD). In the last few years, 1 PLUS i has provided a full range of assistance in developing tailor-made solutions for the practical preparation of recovery plans and resolution strategies for both, institutions operating inside as well as outside Germany. On this basis, 1 PLUS i issued several books and articles to share the gained knowledge and expertise in order to widen the fundamental understanding in recovery and resolution issues.

In general, 1 PLUS i strongly agrees with the entire scope and objectives addressed within the drafted standard to ensure the continuity of access to Financial Market Infrastructure in resolution. As briefly summed-up below, we might draw your attention to only a few slightly amendments:

- We suggest that the definition of “critical shared FMI services” entitles the main factors which are also determining for the definition of “critical shared services”.
- It is necessary that the provider of critical shared FMI services adjusts its rulebooks and contractual arrangements for the case that its customer enters into resolution.
- In our opinion, a stronger interaction between the authority, the FMI receiver and provider is crucial to establish communication channels and gain sufficient information to develop credible contingency plans.
- Critical FMI services which are provided by a FMI intermediary may not be in the scope of the relevant FMI provider. Communication between intermediary and provider is necessary in order to support the risk management of the relevant FMI provider.

We kindly ask you to find more detailed explanations in the attachment of our response. We would be grateful to discuss with you, in further detail, any questions you may have. Please do not hesitate to contact us.

Kind regards,



Dr. Andreas Igl
- Member of Board -



Marcel Krüger
- Consultant -



Tanja Koehler
- Consultant -

09.02.2017 - 1 PLUS i GmbH

Attachment

☰ 1 PLUS i responses to consultation questions

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Attachment: 1 PLUS i GmbH responses to consultation questions

Q1. Does the consultative document appropriately address the tensions that may arise between the various financial stability objectives, with regard to the safety and soundness of providers of critical FMI services on the one hand and to the orderly resolution of the recipients of such services on the other?

We appreciate the suggestions stated in the consultation document and do not have any further comments.

Q2. Do you agree with the overall scope of the guidance and the proposed definitions, in particular the services and functions captured in the definition of ‘critical FMI services’? Should any of the definitions be amended? If so, please explain.

In general, the scope of this guidance meets appropriately the relevant three parties, namely the provider of critical FMI services, the receiver of critical FMI services (mostly banks) and the authorities in charge. Additionally, it might be necessary to analyze the legal structure of critical FMI provider, which could be both banks and non-banks and thus, being subject to different regulations. In the case of non-bank FMI providers, it might be crucial to first establish a general understanding of the topic resolution.

One reason to run a resolution instead of an insolvency is given by the occurrence of at least one critical function within the bank. In a resolution, the bank has to ensure the continuity of critical functions which might depend on the access to critical shared services including critical shared FMI services. As a part of this chain, we recommend to amend the definition of “critical FMI services” in accordance with the definition for “critical shared services” as published by the FSB¹. In a first step, it must be proven whether the shared function is critical or not. In this issue, the criticality will be determined by the substitutability. In other words, the service can only be declared as “critical” if it cannot be easily replaced by other sources.

Due to the scarcity of resources in resolution, we also suggest to establish a ranking of the critical shared FMI services considering the severity of their failure on critical functions and the time until a failure of a critical shared FMI services will lead to a collapse of the critical function.

¹ http://www.fsb.org/wp-content/uploads/r_130716a.pdf?page_moved=1

Q3. What are your views on the proposal in sub-section 1.1 of the consultative document that providers of critical FMI services clearly set out in their rulebooks or contractual arrangements the rights, obligations and applicable procedures in the event of an FMI participant entering into resolution?

We agree that FMI providers should clearly and transparently determine rules or contractual arrangements.

In the scope of these rules or contractual arrangements, we appreciate that the FMI provider has to outline restrictions regarding the termination or the suspension of access to its services by highlighting the relevant legal framework, which depends on the jurisdiction where the FMI provider is incorporated. Following, it should be ensured that the question about the permission to terminate or suspend access to critical FMI services resulting from the legal framework is also addressed in these rules or contractual arrangements.

Furthermore, it would be beneficial to distinguish between the states regular business operations, recovery, resolution and default within the applicable rules and contractual agreements of FMI providers or intermediaries. Amendments due to these different states might be necessary. Hereby, the key challenge is the implementation of trigger points, which lead from one state into another. Our advice is a close collaboration between FMI provider/intermediary respectively the relevant competent authorities of the provider/intermediary and the relevant resolution authority of the failing institution, which will be in charge of the implementation and assessment of the resolution strategy.

Q4. Sub-section 1.1 of the consultative document proposes that the exercise by the provider of critical FMI services of any right of termination or suspension of continued access to critical FMI services arising during resolution of an FMI participant be subject to appropriate procedures and adequate safeguards. What are your views on those procedures and safeguards? In your answer, distinguish where relevant depending on whether the firm that enters resolution continues or fails to meet its payment, delivery and collateral provision obligations to the FMI or FMI intermediary.

During resolution, the availability of critical FMI services is crucial for the success of the resolution strategy. Due to the nature of those critical FMI services, appropriate procedures and adequate safeguards might not exist given by the non-substitutability of these specific services. In our opinion, strong effort should be made to prevent the exercise of termination rights.

After entering resolution, providers of critical FMI services should be informed of the key aspects of the resolution strategy. In particular, the time horizon of the implementation of resolution instruments and possible obstacles, which may lead to a breach of rules and/or contractual arrangement with the FMI provider, should be addressed by the resolution authority.

In order to prevent the termination based on a failure of payment, delivery and/or collateral provision obligations, the resolution authority should pay attention to these obstacles while determining the appropriate resolution strategy. A key supportive element for the resolution authority is the extended information on the operational continuity as mentioned in section 2.2 of the consultation paper.

Q5. Sub-section 1.2 of the consultative document proposes that the general rights, arrangements and applicable procedures of a provider of critical FMI services that would be triggered by entry into resolution of a FMI participant, its parent or affiliate, should be the same irrespective of whether the firm entering into resolution is a domestic or foreign FMI participant. What safeguards should be considered and what measures are needed to ensure a consistent approach is taken across providers of critical FMI services to these safeguards?

We appreciate the thoughts on requirements and safeguards stated in the consultation. In general the mentioned FSB Principles for Cross-border Effectiveness of Resolution Actions are a valid basis for further developments to ensure an appropriate and consistent application.

In our opinion, a possible safeguard would be a protocol similar to ISDA for derivatives but between FMI provider/intermediary and bank. Within this protocol, key elements might be various procedures and requirements depending on the current state (regular business operations, recovery, resolution and default) of the bank. In order to ensure a consistent approach, competent authorities can grant incentives for the participation in this protocol.

Q6. What are your views on the proposal in sub-section 1.4 of the consultative document that providers of critical FMI services should engage with their participants regarding the range of risk management actions and requirements they would anticipate taking in response to the resolution of an FMI participant? Does this strike the right balance between the objectives of orderly resolution and the FMI or FMI intermediary's prudent risk management?

The proposed consultation between the FMI provider and the FMI receiver might not be feasible in practice due to the fact that the final resolution plan will be developed by the resolution authority in charge and only partly be communicated to the FMI receiver beforehand. Under these circumstances, we suggest an enhanced interaction between the FMI provider and the resolution authority.

In the issue of the actions and requirements which a FMI provider will undertake as response to a FMI participant's entrance into resolution, the preferred resolution instruments matter. Notwithstanding, we do not expect that the preferred resolution instrument will be made public. Therefore, it is necessary that the FMI provider generates playbooks which cover the structured instruments bridge institution, sale of business and transfer of assets to a vehicle as well as the financial instrument bail-in. Depending on the resolution instrument, the FMI provider has to take into consideration other factors to ensure the continuity of access to critical FMI services. For instance, in the cases of a bridge

institution and a vehicle, the FMI provider may be required to set up new licenses contracts in a timely manner. In addition, a sale of the business could lead to the connection of critical functions to the already existing FMI services in the buyer's institution. So, an interaction between the FMI providers may be required to enable a fast technical solution. During the bail-in, the FMI participant may change its legal form. Therefore, consequences arising from the new legal form of the counterparty have to be considered.

Q7. Do you agree with the proposal in section 2 of the consultative document that firms should be required to develop contingency plans to facilitate continuity of access in both the lead-up to, and upon entry into, resolution? Does the consultative document address all aspects of the information and analysis that may be required for such contingency plans?

Firms have to ensure that they have access to critical services which they need to maintain critical functions. The development of contingency plans ensures this ongoing access. These contingency plans together with additional information provide the basis for the resolution plan developed by the authorities in charge.

We agree with the proposal in section 2 to set up contingency plans. The scope of these contingency plans should be in relation to various factors, with the complexity of critical functions or the impact of the failure on the financial stability. These contingency plans would tremendously contribute to ensure the ongoing access to critical services while eliminating beforehand possible burdens. To set up a reliable contingency plan, it is necessary to know the additional requirements and actions run by the FMI providers in the different steps of resolution. In this matter, it must be common knowledge, whether the FMI provider requires for example pre-fund resources.

Q8. Are there any aspects of the proposed guidance that should apply differently according to whether access to a critical FMI service is provided directly by an FMI or custodian, or indirectly by an FMI intermediary? If so, please describe with reference to the particular section(s) of the proposed guidance, and include your views on how that section(s) should differ.

Broadly speaking, there should be a difference whether a firm is a direct or indirect FMI participant. The advantage of tiered participation is clear: The wider access to FMI services leads to cost benefits. On the other hand, a high degree of tiering combined with a lack of transparency may cause several problems, which need to be addressed within the guidance. At any time, it should be possible to reconstruct the whole chain.

In this context, short chains would enhance the monitoring and controlling availabilities of the regulator and reduce contagion risk. Another possibility is the limitation of exposures to indirect FMI participants and thus, the encouragement to enter a direct participation. Furthermore, critical FMI service providers have to identify all indirect participants as part of their prudent and sound risk management.

It is necessary to gather basic information to reduce concentration risk and to ensure the continuity of critical FMI services in the case in which a direct participant enters into resolution. In this scenario, the critical FMI service provider have to know how to deal with the indirect participants and on which legal basis the further interaction is based. In practice, it might be challenging to map the whole network for the FMI provider, therefore it could be part of its risk management to set up indirect participation requirements which are valid between the direct participant and its customers to ensure safe and efficient operation. The direct participant should be required to report on a periodical basis to the FMI provider.

Q9. Does the consultative document identify all relevant requirements and pre-conditions that a firm may need to meet to support continuity of access in both the lead-up to, and upon, resolution? What other conditions or requirements, if any, should be addressed?

We appreciate the suggestions stated in the consultation document and do not have any further comments.

Q10. Does the consultative document identify appropriate methods for providing the information and communication necessary for key decision making during the resolution of an FMI participant? Are there additional safeguards that could be put in place that would ensure adequate levels of transparency in the lead-up to, and upon resolution?

We appreciate the suggestions stated in the consultation document and do not have any further comments.