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Secretariat to the Financial Stability Board  
Bank for International Settlements  
Centralbahnplatz 2  
CH-4002 Basel  
Switzerland

**Comments on the Guidance on Continuity of Access  
to Financial Market Infrastructures (“FMIs”) for a Firm in Resolution**

Dear Sirs/Madams:

We, the Japanese Bankers Association (“JBA”), would like to express our gratitude for this opportunity to comment on the consultative document: Guidance on Continuity of Access to Financial Market Infrastructures (“FMIs”) for a Firm in Resolution, issued on December 16, 2016 by the Financial Stability Board (“FSB”).

We respectfully expect that the following comments will contribute to your further discussion.

**[Our responses to 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?

(Our responses)

- The consultative document proposes a set of arrangements required at the level of the providers of critical FMI services which are based on, and consistent with, the “Principles for financial market infrastructures” (hereinafter “PFMI”), published by CPMI/IOSCO in April 2012. We agree with the intent of Principle 2 “Governance” of PFMI referred in sub-section 1.1 of the consultative document that “FMIs specifically should have governance arrangements that are clear and transparent, promote the safety and efficiency of the FMI, and support the stability of the broader financial system, other relevant public interest considerations, and the objectives of relevant stakeholders.” In case providers of critical FMI services terminate or suspend access

of financial institutions in the entry into orderly resolution, they should consult with relevant supervisory authorities of such financial institutions beforehand.

- At the same time, consistency with Principle 21 “Efficiency and effectiveness” of the PFMI should be ensured as well. Specifically, explanatory note 3.21.1 to the Principle mentions that “an FMI that operates inefficiently or functions ineffectively may distort financial activity and the market structure, increasing not only the financial and other risks of an FMI’s participants, but also the risks of their customers and end users.” This should be taken into consideration in the guidance.
- It seems reasonable to a certain extent for providers of critical FMI services to require modification of terms and conditions in exchange for continuance of access to FMIs in the orderly resolution of the financial institutions. Nonetheless, there is a concern also in this respect that if new contractual arrangements (modification of terms and conditions) with financial institutions introduced by providers of critical FMI services are overly conservative, transaction costs and liquidity risks, etc. of FMI participants may be increased and thereby might cause adverse effects on the financial system. Adequate consideration should be given by providers of critical FMI services (and the relevant supervising authorities) so as not to shrink transaction volume of FMI participants and their customers.

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?

(Our responses)

**i. Procedures of arrangements required at the level of providers of critical FMI services and financial institutions**

- The guidance should clarify and set out procedures of those arrangements both for providers of critical FMI services and FMI participants (financial institutions) in order to ensure continuity of access to the FMIs when a financial institution enters into resolution.
- The consultative document requires that providers of critical FMI services engage with financial institutions to set out the rights, obligations and applicable procedures in the event of a financial institution entering into resolution, and then to establish additional requirements applicable to financial institutions. Financial institutions, on the other hand, are required to develop contingency plans to facilitate continuity of access to FMIs engaging the providers of critical FMI services.
- However, as the consultative document does not clarify or set out the procedures at the level of providers of critical FMI services and financial institutions, necessary arrangements and actions proposed in this consultative document may not be processed smoothly. In this regard, it is presumed that providers of critical FMI

services would request FMI participants to pledge liquidity buffer, and to set terms and conditions in the case of resolution, which may be more or less the same for most of the financial institutions. When financial institutions develop contingency plans, it is indispensable that providers of critical FMI services fix requirements to financial institutions beforehand. If providers of critical FMI services and financial institutions negotiate individually, it might require more time and workload than necessary. Therefore, it is preferable for a provider of critical FMI services and its participants to have discussion together to sort out tasks, rather than bilateral discussion between each provider of critical FMI services and each participant. In terms of smooth implementation of the proposed guidance, the guidance should clarify and set out specific procedures for financial institutions and providers of critical FMI services.

- Furthermore, for ensuring an orderly resolution, prompt actions and cooperation among all responsible-parties, that is, providers of critical FMI services, financial institutions and their relevant authorities, would be necessary in the lead-up to resolution. While it is essential for financial institutions to report to supervisory authorities in normal circumstances (e.g. status of use of FMIs) and to develop contingency plans, it would also be useful if the guidance provides playbook for actions and communications among the three parties in resolution.

## **ii. Communication between providers of critical FMI services and financial institutions**

- The guidance assumes engagement between providers of critical FMI services and financial institutions in order to respectively take initiatives to ensure an orderly resolution.
- However, since there are a number of combinations of providers of critical FMI services and financial institutions, it is expected that a considerable amount of time will be required for carrying out all combinations of communication on an ad-hoc basis.
- In order to ensure efficient communication and to proceed with arrangement for the guidance, it is effective to clarify a framework or procedure regarding the engagement among them. For example, it is considered effective that relevant authorities of financial institutions and providers of critical FMI services arrange opportunities to facilitate communications between financial institutions and providers of critical FMI services.

## **iii. Communication between providers of critical FMI services**

- When developing contingency plans detailing approaches to maintain access to the critical FMI services, financial institutions should take into account continuity of access to other FMI services (e.g. since securities can be settled only when central counter party (“CCP”) gives a settlement instruction to central securities depository (“CSD”), it is necessary to maintain access to both CCP and CSD in order to continue securities settlement). Therefore, in consideration of interconnectivities of multiple FMI services, new arrangements required by a provider of critical FMI services to

financial institutions should be consistent with the ones required by providers of other FMI services.

**iv. Arrangements in accordance with resolution regimes**

- The PFMI already sets out principles for providers of critical FMI services. For example, CCPs are required contributions of default funds in preparation for losses arising from failure of clearing participants and allocation of margin to cover exposures. Therefore, it is considered that further risk management-related requirements for FMIs would be excessive.
- Particularly, assumption of those financial institutions, which will adopt Single Point of Entry (“SPE”) approach (“SPE financial institutions”), is that their operating banks will not be in default and continue its business even in the case of group resolution by development of internal TLAC framework. On the other hand, providers of critical FMI services have already prepared for measures for defaulted FMI participants, in accordance with Principle 13 of the PFMI (Participant-default rules and procedures), such as procedures for fulfilling obligations and compensation of liquidity by other FMI participants. Compared with the PFMI, the guidance requires actions under the lower risk situation.

Given this, what needs to be additionally considered by SPE financial institutions would be limited to removal of the cross-default clause, contractual arrangements agreeing not to terminate access to FMIs in a resolution and compliance with the minimum liquidity buffer.

- On the other hand, in case of Multiple Point of Entry (“MPE”) approach, operating banks will be in default. In this case, all contracts, including with FMIs, will be triggered at the default clause, and critical economic functions and related systems for ensuring access to FMIs are assumed to be transferred to a bridge institution. Therefore, it is understandable that it is difficult to ensure continuity of access only to the extent prescribed in the PFMI and thus additional risk management actions are required of the providers of critical FMI services.

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.

(Our response)

- It is not necessary to apply the guidance to FMI intermediaries. It is sufficient for FMI intermediaries: (i) to provide information on indirect participant of FMIs being accessed; and (ii) to review a contractual agreement between the FMI intermediaries and the indirect participants.

(Rationale, etc.)

- In general, contracts between FMI intermediaries and financial institutions stipulate that FMI intermediaries do not assume risk or loss which providers of FMI suffer as a result of negligence/default of the user financial institutions.
- In this respect, inherent risk of the FMI intermediary is low because its role is an agent for settlement with data received or funds secured in advance from the financial institutions as indirect participants.

Therefore, regarding access to an FMI through an FMI intermediary, it will be enough, in order to maintain access even in the event of a resolution of financial institution, if the FMI intermediary: (i) submits transaction information of the indirect participants to the providers of FMI services; and (ii) makes contractual arrangements agreeing not to terminate the contract if orderly resolution regimes are applied.

- Where there are any reasonable reasons for a provider of critical FMI services to individually build up liquidity reserve, the provider of critical FMI services may request the indirect participants to provide such reserve via FMI intermediaries.

#### **[Other Comments]**

##### **(1) Implementation deadline**

- It should be recognized that financial institutions would need a considerable period of time to address the proposed guidance, and therefore, deadline should be set in a flexible manner.
  - Financial institutions are required to: (i) conduct a fact-finding for provision of information to supervisory authorities; (ii) engage and consult with providers of critical FMI services; and (iii) develop contingency plans. It will take time to make these arrangements.
  - It is assumed that a considerable period of time will be needed in particular for engagement with providers of critical FMI services mentioned above as (ii), because there are a number of combinations of providers of critical FMI services and financial institutions.
  - Therefore, considering burdens of FMIs and financial institutions, relevant authorities should set the implementation deadline in a flexible manner.

##### **(2) Continuity of access expectations and requirements applicable to firms (section 2, p.17)**

- Consistent arrangements should be made by assumed resolution regimes.
  - While the consultative document proposes that financial institutions should develop contingency plans, it is considered that granularity of the plans should vary according to financial institutions' resolution strategies (i.e. SPE or MPE approach) or corporate structure (i.e. whether the resolution entity has accesses to FMIs).

- For example, in the case where SPE resolution regime is applied and its holding company as a resolution entity does not have an access to FMIs, its risk/corporate management framework is established under the assumption that its operating bank will not be in default even in default of resolution entity. Therefore, it is particularly important to ensure FMI accesses by addressing contractual arrangements (i.e. removal of cross-default/change of control clauses and set of a clause that prevents termination of access to FMI services in an orderly resolution) as well as satisfaction of liquidity conditions (additional requirements of financial institutions entering into resolution). Therefore, more emphasis should be put on contractual arrangements and satisfaction of liquidity requirements when engaging with providers of critical FMI services and preparing a contingency plan. Please note that the liquidity requirements may not be a major issue in those jurisdictions where there is a statutory temporary liquidity support framework for critical functions.
- On the other hand, when MPE resolution regime is applied, it is assumed that operating banks will be resolved, that all contracts including with providers of critical FMI services will be applicable to default covenants, and that part of business activities/assets will be transferred to a bridge institution, as mentioned in above “iv” to the question 3. In this case, complicated operations will be necessary and thus the detailed contingency planning is highly required.
- Given the aforementioned difference in risk for continued access to FMIs, the guidance should distinguish and describe the specific arrangements in line with the resolution regime, SPE and MPE. In particular, home authority of a financial institution should determine granularity for contingency plans in a flexible manner, which is in line with the financial institution’s resolution strategy or corporate structure, through consultation with providers of FMI services and their relevant authorities.

### **(3) Contingency planning to meet conditions of access in resolution (section 2.3, p.19)**

- Stress scenario analysis in contingency plans should be limited in line with the resolution strategies. Excessively detailed analysis should not be required.
  - As described in (2), risks of continued access to FMI services differ depending on financial institutions’ resolution strategies and corporate structures. Therefore, stress scenarios prescribed in contingency plans should be reasonable and limited.
  - In developing contingency plans, financial institutions are required to consider expected responses of providers of critical FMI services under different scenarios, and to encourage better understanding of providers of critical FMI services. However, according to examples of resolution scenarios described in the consultative documents, it seems that the guidance requires financial institutions to analyze beyond the scope of the assumption in the orderly resolution regime, such as a credit rating downgrade after the entry into resolution and non-fulfillment of settlement obligations by the operating bank.

- In developing contingency plans, it is assumed that financial institutions will engage with providers of critical FMI services and share awareness of risks, etc. If they engage on the premise of broad and overly deep scenario analysis, FMIs may impose extra liquidity reserve or transaction fees, which may result in excessive increase of settlement cost across the overall financial system.

**(4) Balancing the objectives of relevant authorities for providers of critical FMI services and resolution authorities of FMI participants (section 3.1, p.23)**

**i. Supervisory authorities should ensure review of terms and conditions by providers of critical FMI services will not be excessive in order to prevent adverse effects on settlement transactions.**

- Financial institutions in a host country decide ways of access to FMIs, either directly or indirectly, depending on the economic rationality such as transaction volume and system cost. Settlement fees, etc. charged to their customers are determined based on this.
- In many cases of indirect access to FMIs in host countries, G-SIBs headquartered in the countries act as FMI intermediaries, but they are not actually exposed to significant risks. Nevertheless, it is concerned that FMI intermediaries may ask financial institutions for excessive reserves and charges in accordance with the proposed guidance, which are far from the level of settlement risks arising from the resolution regime. As a result, the current economic rationality may change significantly, and lead to declining of profitability of financial institutions in the host country and ultimately to influence on settlement fees charged to customers on a global basis.
- In order to ensure that review of terms and conditions pursuant to the proposed guidance will not be excessive, it should be explicitly described in the guidance that the review needs to be consistent with risks for continued access to FMIs. Furthermore, it would be necessary to develop a supervisory authorities' monitoring framework.

**ii. Initiative by supervisory authorities should be considered with respect to engagements between providers of critical FMI services and financial institutions.**

- The draft guidance requires providers of critical FMI services and financial institutions to communicate each other to ensure continuity of access to FMIs in the entry into resolution. However, irrespective of direct or indirect access by FMIs, it is sometimes difficult for financial institutions to request providers of critical FMI services for modification of the termination clause or for changes to adequate terms and conditions, given the power balance in their relationships. In this regard, the relevant authorities for both providers of critical FMI services and financial institutions should cooperate to monitor whether negotiations between them are fair and their terms and conditions are adequate considering resolution strategies adopted in each jurisdiction. If such negotiations or terms and conditions were excessively inadequate in light of respective resolution strategies, it is considered that a

framework should be established in which relevant supervisory authorities encourage providers of critical FMI services and financial institutions to adjust them.

Sincerely,

Handwritten signature in blue ink, consisting of the characters '高木 伸' (Takagi Shin).

Shin Takagi, Vice Chairman & Senior Executive Director