



Via E-Mail [fsb@bis.org](mailto:fsb@bis.org)

15<sup>th</sup> October. 2013

The Financial Stability Board (FSB)

Dear Board Members,

***The Clearing Corporation of India Ltd, Mumbai, India  
Response Consultative Document on Application of the Key Attributes of  
Effective Resolution Regimes to Non-Bank Financial Institutions Aug '13***

We congratulate FSB for publishing a comprehensive document which would provide guidance to all involved in planning recovery and resolution of MFIs. FSB's October 2011 document on Key Attributes of Effective Resolution Regimes for Financial Institutions and July '13 documents for guidance of SIFIs have helped development of common understanding on the subject and this document seeks to take it forward by bringing critical issues on clearer focus.

2. We operate in India as a CCP for OTC financial market products since 2002 as an authorized Payment & Settlement System Service Provider authorized by Reserve Bank of India, the central bank of India. We presently provide CCP clearing for mainly institutional trades in Government Securities, Foreign Exchange – both spot and forward trades in Rupee/US Dollars, trades in domestic money market through our own product Collateralised Borrowing & Lending Obligation (CBLO). We are also in the process of offering CCP clearing of Indian rupee denominated trades in Interest Rate Swaps by using a trade data warehouse for such swaps created by us in Aug 2007.

3. Although the document is comprehensive, we would like to provide a few suggestions and observations for your consideration:

(i) The document in para 1.1 stresses continuity and timely completion of critical FMI functions including clearing and recording. However, if resolution process is initiated, the FMI would typically suspend assumption of additional liability by freezing positions at the levels already accepted. The FMI therefore cannot be expected to continue receiving, recording and clearing transactions. If a bridge institution is created as a part of resolution process, the bridge institution can however do so.

Moreover, as mentioned in the CPSS-IOSCO consultative document on Recovery of FMIs (CPSS 109), recovery generally happens in the shadow of resolution. It is likely that the FMI will then operate with diminished resources as certain lines of credit or other facilities/arrangements could be withdrawn by service providers. This can have impact on settlements as well.

(ii) In para 4.12, it has been suggested that FMI should enter into advance agreement with a third party institution. It would appear to be impractical to do so. Such an arrangement would require that the third party institution is fully aligned with all business processes, arrangements etc. of the FMI which may not be possible.

(iii) In respect of observation in Para.1.2 of Annexure II, the intention behind stating that the entry into resolution of an FMI participant should not lead to an automatic termination of its participation in the FMI should not be construed as any impingement of the FMI's right to suspend such participant for violation of its rules and procedures.

(iv) On the Questions for Consultation, our responses are as under:

### **Part I of the Draft Guidance: Resolution of Financial Market Infrastructure**

Q1. Does the draft guidance adequately cover the principal considerations that are relevant to the resolution of each class of FMI (CCPs, CSDs, SSS, PS and TRs)? Would it be helpful if the guidance distinguished more between different classes of FMI? If so, please explain.

Response: The guidance is broad enough to cover the principal considerations and it has reinforced the idea of continuity of critical FMI functions as the core objective along with Financial Stability. However, as the financial exposures on CCPs are of relatively longer term in nature, if a resolution of a CCP is required, it will pose a very different challenge as compared to resolution of all other types of FMIs e.g., resolution authorities for CCPs would possibly need much more in depth knowledge of the market, participants, likely behaviour of various stakeholders where CCP is likely to be entering into resolution, porting of positions of indirect participants, possible legal challenges etc. Hence, it would be desirable to provide additional guidance with specific focus on resolution of CCPs.

It is also inevitable that there will remain imperfections and cross border legal incompatibility in case of CCPs having operations across borders which will not get addressed in the foreseeable future. To address these issues, sufficient discretions are required to be allowed to the Resolution Authorities and their actions are to be in line with the expectations of the Supervising Authorities. It will be desirable that the guidance looks into these issues in greater detail and provide a framework.

Q2. Should any further distinction be made in the draft guidance, for the purposes of applying the Key Attributes, between types of FMI that assume credit risk through exposures to participants and those that do not? If so, for which provisions is that distinction relevant?

Response: Distinction should be made between CCPs and othewr types of FMIs. please refer to Q1 above.

Q3. Are the additional statutory objectives for the resolution of FMI (paragraph 1.1) appropriate? What additional objectives (if any) should the draft guidance include, relating either to FMIs generally or specific classes of FMI?

Response: As both Financial Stability objective and the objective of continuity of critical FMI functions are to be achieved so that the market does not get unduly impacted and that the portability of indirect participants are also achieved, if required, with least possible delay, it is necessary to have the objectives and conferred additional powers transparently understood by all stakeholders and are taken into account.

Q4. Is it appropriate to exclude FMIs that are owned and operated by central banks from the scope of application of the Key Attributes and this guidance (paragraph 2.1)?

Response: As long as Central Bank ensures that the objective of continuity of critical FMI functions is achieved, it is not necessary to seek for resolution of FMIs owned and operated by the Central Banks. However, resolvability of such FMIs should be assessed periodically and the results should be available to various stakeholders.

Q5. Should resolution authorities have a power to write down initial margin of direct or (where appropriate) indirect participants of an FMI in resolution (paragraph 4.8)? If so, should the power be restricted to initial margin that is not 'bankruptcy remote' and may be used to cover the obligations of participants other than the participant that posted it? What are the implications of such a power for FMIs and participants? Are any further conditions appropriate in addition to those specified in paragraph 4.9?

Response: In case the loss originates from failure of a clearing participant, writing down of variation margin should be usually adequate to meet the shortfall. However, if the origin of loss is from operational failure or from failure of settlement bank, instead of writing down initial margin of both direct & indirect participants, use of Assessment Power to distribute loss upto the maximum permissible assessment limit would be a better option.

Q6. Should the Annex explicitly restrict resolution authorities from interfering with the netting rights of FMI participants (for example, by splitting a netting set through partial transfer of positions in a CCP or partial 'tear up' of contracts)? What is the possible impact on participants' risk management, accounting reporting or regulatory capital requirements if netting rights can be interfered with in resolution, and how might any such impact be mitigated?

Response: In the interest of least disruption, netting rights of FMI participants should not be interfered with, even by Resolution Authorities.

Q7. Does the draft guidance (paragraphs 4.1 and 4.2) adequately address the specific considerations in the choice of the resolution powers set out in KA 3.2 to FMIs? What additional considerations (if any) regarding the choice of resolution powers set out in KA 3.2 that should be addressed in this guidance?

Response: It would be better if the aspect of overriding rights of shareholders, establishment of a temporary bridge institution, establishing separate asset management vehicle etc. are again reiterated.

Q8. Are the conditions for entry into resolution of FMI (paragraph 4.3) suitable for all classes of FMI? What additional conditions (if any) would be relevant for specific classes of FMI?

Response: While as a broad guideline, the conditions are adequate. However, on the ground, interpretation of when an FMI is no longer viable can lead to confusion. Moreover, for a CCP, this issue will probably be decided based on assessment and would assume very critical importance. It would, therefore, be better if clear guidance is provide for each type of FMIs.

Q9. Does the draft guidance (and paragraphs 4.4, 4.8 and 4.9 in particular) deal appropriately with the interaction between the contractual loss-allocation arrangements under the rules of certain classes of FMI and the exercise of statutory resolution powers?

Response: The loss allocation related guidance appears to be adequate,

Q10. Should contractual porting arrangements be recognised in the draft guidance on the transfer of critical functions (paragraphs 4.11 and 4.12)?

Response: The guidance appears adequate.

Q11. Are there any other FMI-specific considerations regarding the application of any of the 8 resolution powers set out KA 3.2 that should be covered in this guidance?

Response: FMI specific considerations have been listed out in a brief manner and this should be adequate.

Q12. Does the draft guidance (paragraphs 5.1 and 5.2) deal appropriately with the considerations that are relevant to the decision whether to stay the exercise of early termination and set-off rights by FMI participants on the entry into resolution of the FMI? Should the guidance distinguish between different classes of FMI in this regard?

Response: : Yes. This would be applicable only for CCPs and to some extent to SSSs.

Q13. Are loss-allocation arrangements under FMI rules reflected appropriately in the application of the “no creditor worse off” safeguard in FMI resolution (paragraph 6.1)?

Response: Yes

Q14. What additional factors or considerations (if any) are relevant to the resolvability of FMIs, or particular classes of FMI (paragraphs 10.3 and 10.4)?

Response: For CCPs, the approach should be different from other FMIs. Moreover, regulatory support expected, if any, should be clearly documented. It would be ideal to have resolution regime for MFIs created through legal enactments in all jurisdictions so that any possibility of frivolous legal challenges causing disruption in resolution process could be avoided.

Q15. Are there additional matters that should be covered by resolution plans for FMIs or particular classes of FMI (paragraphs 11.6 and 11.7)? If yes, please elaborate.

Response: : Guidance for Resolution Plans provided in the document is adequate

Q16. Are the proposed classes of information that FMIs should be capable of producing (paragraph 12.1) feasible? Are any of the proposed classes of information unnecessary, duplicative or redundant? What additional classes of information (if any) should FMIs be capable of producing for the purposes of planning, preparing for or carrying out resolution?

Response: For interoperability arrangements, information on exposures to linked CCPs and collaterals provided to and received from such CCPs should be available.

Q17. Are there any other issues in relation to the application of the Key Attributes to FMIs or particular classes of FMI that it would be helpful for the FSB to clarify in this guidance? If yes, please elaborate.

Response: Roles of Regulators and the likely support from Regulators like collateralised liquidity support etc. should be clearly documented.

## **Part II of the Draft Guidance: Resolution of Systemically Important FMI participants**

Q18. Does the draft guidance achieve an appropriate balance between the orderly resolution of FMI participants and the FMI's ability to manage its risks effectively?

Response: There is no conflict. However, FMI's should take actions based on its risk mitigation needs and by keeping Financial Stability objective into consideration. Coordination between various stakeholders would also be of help.

Q19. What actions of the FMI in relation to failing participants could hamper its orderly resolution? How could the impact of such actions on orderly resolution be mitigated or managed?

Response: Close out of positions and transfer of such positions to other clearing participants through auctions or otherwise by a CCP can hamper resolution of the participant which is in default. Moreover, enforcing securities/collaterals of such failing participants which have been obtained by them through collateral transformation could pose difficulties.

20. Are the safeguards set out in the guidance (paragraph 1.3) adequate as regards the conditions and requirements for maintaining access of a firm in resolution or admitting as a new member an entity to which that firm's activities have been transferred? If not, what additional safeguards should be included in the guidance?

Response: Additional safeguards could be set in the form of stipulated limits for ownership structure, management, capital etc. of such bridge institution.

21. Are there any other issues in relation to the handling of the failure of FMI participants that it would be helpful for the FSB to clarify in this guidance? If yes, please elaborate.

Response: Regulatory stance in respect of resolution of any FMI participant which is a regulated entity could be of significance.

*4. If any information/clarification about this submission is needed, please feel free to contact Mr Siddhartha Roy, Chief Risk Officer, The Clearing Corporation of India Ltd., Mumbai, India at +91 22 6154 6411 or via sroy@ccilindia.co.in or Mrs Indrani Rao, Chief Forex Officer, The Clearing Corporation of India Ltd., Mumbai, India at +91 22 6154 6461 or via irao@ccilindia.co.in*

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