THE HONG KONG ASSOCIATION OF BANKS
香港銀行公會

Room 525, 5/F., Prince's Building, Central, Hong Kong
Telephone: 2521 1160, 2521 1169 Facsimile: 2868 5035
Email: info@hkab.org.hk Web: www.hkab.org.hk

香港中環太子大廈5樓525室
電話：2521 1160, 2521 1169 圖文傳真：2868 5035
電郵：info@hkab.org.hk 網址：www.hkab.org.hk

16 February 2017

By email: fsb@fsb.org

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

Dear Sirs

Consultations on Proposed Guidance to Support Resolution Planning and Promote Resolvability

We refer to the consultative documents on "Guiding Principles on the Internal Total Loss-absorbing Capacity of G-SIBs ('Internal TLAC')" and "Guidance on Continuity of Access to Financial Market Infrastructures ("FMIs") for a Firm in Resolution" issued on 16 December 2016.

On behalf of our members, we set out in the enclosed annexes our comments on the abovementioned consultative documents for your consideration.

We hope you find our comments useful. Should you have any questions, please contact our Manager Ms Emily Ngan at (852) 2526 6080 or our Officer Ms Helen Ng at (852) 2567 1363.

Yours sincerely

Celia Shing
Secretary

Enc.

c.c. Mr. Eamonn White, Head (Resolution), Hong Kong Monetary Authority

Annex 1

Submission of The Hong Kong Association of Banks in response to

the Financial Stability Board's 16 December 2016 Consultative Document on

Guiding Principles on the Internal Total Loss-absorbing Capacity of G-SIBs ('Internal TLAC')

16 February 2017

Introduction

The Hong Kong Association of Banks (***HKAB***) was created by The Hong Kong Association of Banks Ordinance in 1981, which among other things provides a framework for the Hong Kong Government to exchange views with the banking sector for the further development of the industry. Every fully licensed bank operating in the Hong Kong Special Administrative Region must be a member of HKAB and subject to HKAB's rules. The roles of HKAB include being a focal point for consultation on law reform, new legislation and regulatory matters.

HKAB has reviewed the Consultative Document on Guiding Principles on the Internal Total Loss-absorbing Capacity of global systemically important banks (***G-SIBs***) (the ***Guiding Principles***) issued by the Financial Stability Board (***FSB***) on 16 December 2016 (the ***Consultative Document***) and has received feedback from members of HKAB on the Consultative Document. This paper, which was prepared with the assistance of international law firm Freshfields Bruckhaus Deringer, sets out the views of HKAB based on the feedback it has received from HKAB members.

Questions from the Consultative Document are repeated below in bold and italicised text, with HKAB's views set forth following each question.

General Comments

In respect of the terminology used in the Guiding Principles, for clarity HKAB would suggest that the terms "home authority" and "host authority" are defined in the Guiding Principles. In the context of the Guiding Principles, HKAB's understanding is that the term "home authority" means each resolution authority of a G-SIB's resolution entities (in the case of a Multiple Point of Entry Strategy) rather than only the resolution authority of the G-SIB itself; and "host authority" means each resolution authority of the material sub-group of the resolution entity (where the material sub-group is located in a different jurisdiction to the resolution entity).

HKAB acknowledges that the home and host authorities' interests need to be balanced and suggests that the FSB should go further to promote the objectives of cross-border resolution, including having the home authority lead resolution planning and execution and regulatory co-operation and collaboration, especially in setting internal TLAC requirements.

Responses to Consultation Questions

Question 1: ***What factors should the relevant authorities take into account when determining the composition of material sub-groups and the distribution of internal TLAC between the entities that form the material sub-group (guiding principle 2)?***

While the host authority should ensure there are no operational or legal barriers which would prevent or restrict the use of internal TLAC to recapitalise subsidiaries in the material sub-group of a resolution entity, the host authority should also consider subsidiaries which are not wholly-owned by the material sub-group as the distribution of the internal TLAC may become uncertain if it is dependent on the approval of minority shareholders.

In the case of publicly-listed subsidiaries which are resolution entities or part of a material sub-group, the home authority also should take into consideration other regulatory requirements and/or legal considerations, such as any applicable stock exchange listing rules governing connected transactions.[1]

HKAB agrees that the home authority should initiate and coordinate the process for identifying material sub-groups and the annual review of the list of material sub-groups with the host authorities and the Crisis Management Group (***CMG***). However, it should be clarified that it is the home authority which initiates the process rather than host authorities making proposals.

If a new sub-group is identified as material, HKAB's view is that banks must be allowed adequate time to meet the internal TLAC requirement to reflect the addition of the new material sub-group.

Similarly, if a material sub-group ceases to be "material", HKAB's view is that such sub-group should cease to be subject to any internal TLAC requirements (i.e., it should be treated in the same way as if it had never been designated as a material sub-group). HKAB is concerned with the implications of the following statement in the Consultative Document: "*the sub-group may continue to be subject to local TLAC or other requirements imposed by the host authority as part of domestic regulation, which will need to be taken into account when internal TLAC instruments are called or redeemed.*"

Question 2: *What are your views on the treatment of regulated or unregulated non-bank entities as set out in guiding principle 4? If such entities were included within a material sub-group, how should the relevant authorities calculate an internal TLAC requirement?*

HKAB generally supports the proposed treatment of regulated or unregulated non-bank entities as set out in Guiding Principle 4, which is that such entities should be designated or included in material sub-groups only to the extent that their inclusion is necessary to ensure that the resolution strategy for the resolution group is credible and feasible, and that continuation of the entities, or of the services they provide, cannot be achieved through alternative arrangements.

However, HKAB believes that the internal TLAC requirement calculated in terms of risk-weighted assets (***RWA***) should be applied to banking entities only (so as to be consistent with the current Basel framework, in which the RWA calculation is only applicable to banks).

HKAB supports the proposition that alternative arrangements should be discussed and agreed with resolution authorities so as to achieve the continuity of regulated non-bank entities in a resolution.

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[1] In Hong Kong (and in a number of other markets), connected transactions are transactions with connected persons, and transactions with third parties that may confer benefits on connected persons through their interests in the entities involved in the transactions. Connected transactions include both capital and revenue nature transactions. They may be one-off transactions or continuing transactions. The general requirements for connected transactions include disclosures in announcements, circulars and annual reports, and shareholders' approval. Persons with material interests cannot vote on the resolution approving the transaction. Continuing connected transactions also require annual reviews by the listed company's independent non-executive directors and its auditors.

In addition, and specifically in relation to unregulated non-bank entities in material sub-groups that provide critical shared services such as IT infrastructure, software, and/or business supporting functions, HKAB supports the proposition that resolution authorities should consider alternative arrangements other than formal requirements on additional loss-absorbing capacity. Such shared service entities will support the group resolution strategy and it would be unduly burdensome to require such entities to be subject to internal TLAC requirements. As such, HKAB believes that they should not be subject to the internal TLAC principles.

Question 3: ***Do you agree with the roles of home and host authorities in relation to the host authority's determination of the size of the internal TLAC requirement, as set out in guiding principles 5 and 6? What additional factors, if any, should the host authority take into account when setting the internal TLAC requirement?***

HKAB agrees that there should be consultation between the home and host authorities on the size of the internal TLAC requirements. Furthermore, minimum internal TLAC requirement should be determined at the lower end of the 75% - 90% range and there should be no specified, presumed maximum.

Internal TLAC requirements for a material sub-group should generally not exceed such a requirement for an equivalent local bank, so as to ensure a level playing field in that jurisdiction (for banks whose headquarters are based in the European Union, taking into account the 'external minimum requirement for own funds and eligible liabilities' (or MREL) of the resolution entity on which the material sub-group depends).

HKAB recognises the challenge of coordinating the internal TLAC requirements between different material sub-groups and aligning these requirements with a G-SIB's requirement, however, HKAB's view is that the following principle (as set out in the "Principles on Loss-absorbing and Recapitalisation Capacity of G-SIBs in Resolution – TLAC termsheet") should be maintained: "*…if the sum of Minimum TLAC requirements of the resolution entities within the same G-SIB is above the Minimum TLAC requirement which would apply if the G-SIB were to have only one resolution entity, the G-SIB's home and relevant host authorities, meeting in the CMG, shall discuss, and where appropriate and consistent with the G-SIB's resolution strategy, agree an adjustment to minimise or eliminate that difference.*"

HKAB notes that Guiding Principle 6 states that "*it would be beneficial to maintain some TLAC at the resolution entity…*". HKAB's concern is that this could be interpreted to mean that some kind of cash pool needs to be maintained, which may not be practical or efficient for the following reasons:

(i) At the point of resolution, if the TLAC is not pre-positioned, the board of the holding company would need to consider its fiduciary duties when it commits any cash to the troubled subsidiary. This is akin to a new equity investment, and very different from the conversion of an existing debt holding. Determining that this would be an appropriate investment may be feasible in a recovery scenario but it becomes more problematic in resolution where the value of the asset being acquired is more questionable.

(ii) Cash which is retained in a holding company is not being economically employed as it will need to be held as High Quality Liquid Assets (***HQLA***). This represents a further burden on both the relevant bank and the wider economy, which should be avoided.

As a result, where a holding company issuing external TLAC has fulfilled its obligation to meet the internal TLAC requirements established for the relevant material sub-groups and subsidiaries, it should be able to deploy the balance of funds raised from external TLAC issuance as TLAC or in other forms as it sees fit.

As mentioned in the General Comments section above, the Guiding Principles emphasises the role of host authorities. HKAB would prefer to see more balance in the final Guiding Principles to underscore the collaborative group approach to cross-border resolution agreed in the CMGs and led by home authorities.

For example, in cases where the sum of internal TLAC requirements exceed the resolution group's external minimum TLAC requirement, home and host authorities should be given the flexibility to work together through the CMG to agree on lower internal TLAC requirements.

Moreover, the final Guiding Principles should provide for a formal dispute resolution mechanism at the level of the CMG to resolve potential issues between home and host authorities. Overall, the setting of internal TLAC requirements should, to the extent possible, be a collaborative process conducted within the CMG to ensure coherence of resolution plans.

Question 4: ***How should TLAC at the resolution entity that is not distributed to material sub-groups ('surplus TLAC') be maintained to ensure that it is readily available to recapitalise any direct or indirect subsidiary, as required by the TLAC term sheet (guiding principle 7)?***

HKAB believes that external TLAC requirements could be designed from a "top-down" approach, with a total external TLAC requirement determined at the consolidated level, and distributed in the form of internal TLAC to material sub-groups only. Thus, there may be circumstances where the consolidated external TLAC requirement exceeds the sum of internal TLAC for material sub-groups. Management buffers also could be employed.

Alternatively, a parent company's external TLAC requirement could be designed to be equal to the sum of the internal TLAC requirements of its material sub-groups, with no TLAC required to support assets that are maintained outside the material sub-groups. There may, however, be circumstances in which the external TLAC issued exceeds the external TLAC requirement.

In respect of management buffers, HKAB would expect that a parent company could elect to over-issue external TLAC in order to ensure that it has a suitable management buffer against the minimum requirements. HKAB's view is that this is likely to be an approach which resolution authorities should encourage, given the potential timing issues involved in the issuance of new TLAC instruments and the difficulties which may arise if the minimum requirements are breached.

HKAB does not believe that banks should be disincentivised from building external TLAC buffers. However, holding the proceeds of any over-issuance of external TLAC as cash or HQLA at the holding company level would be financially inefficient for the relevant financial group since the yield on such investments would likely be lower than cash which is deployed in mainstream business activities. Financial groups should be able to deploy the cash as they see fit, taking into account (i) the potential requirements for such cash to be redeployed as internal TLAC depending on changing requirements; and (ii) the potential consequences if external or internal TLAC requirements are not met.

In relation to all-inclusive issuance, in some jurisdictions and for some entities all senior debt issued by the holding company for funding purposes would be eligible to be treated as external TLAC, and it is possible that the TLAC requirements could be significantly exceeded. In these circumstances, HKAB believes it would be inappropriate if all surplus TLAC had to be held at the holding company level as its primary purpose would be to provide funding for the group and it would be inappropriate to force an adjustment in this top-down funding model, which may in fact be detrimental to resolution.

Each group should be allowed to determine the way in which it meets the "readily available" requirement, to the satisfaction of its CMG and applicable resolution authorities.

HKAB also would like to request that, in formulating the framework for the internal TLAC regime, the needs of a financial group as a going concern should also be considered (e.g., commercial, treasury and tax concerns should be taken into account). The final Guiding Principles should, to the extent possible, avoid any implication of the need to do "dollar tracing" or impose undue constraints on the designation or form of funds within the financial group.

Question 5: ***What are your views on the composition of internal TLAC, as set out in guiding principle 8? In particular, should there be an expectation of the inclusion within internal TLAC of debt liabilities accounting for an amount equal to, or greater than, 33% of the material sub-group's internal TLAC?***

HKAB does not support the proposal that a minimum of 33% of the material sub-group's internal TLAC may need to be in the form of debt liabilities (the ***33% Requirement***).

HKAB takes the view that a material sub-group should be able to utilise the existing regulatory capital instruments from the resolution entity to satisfy the internal TLAC requirement. This includes any retained earnings in the material sub-group.

HKAB notes that the 33% Requirement could lead to a situation where the material sub-group needs to issue additional internal TLAC beyond what is required by the relevant host authority. The 33% Requirement also seems to contradict Guiding Principle 9, which states that collateralised guarantees can be substituted as on-balance sheet internal TLAC.

Question 6: ***What are your views on the potential benefits or drawbacks of different approaches to the issuance of internal TLAC instruments as set out in guiding principle 10, and what steps could be taken to mitigate the drawbacks that you have identified?***

HKAB notes that direct and daisy-chain issuance structures are not the only possibilities. Instead of prescribing specific approaches to the issuance of internal TLAC, banks should be allowed flexibility to adopt alternative approaches, provided that such approaches credibly support the bank's resolution strategy (i.e., appropriate loss absorption / recapitalisation of the applicable resolution entities).

Question 7: ***Should the FSB conduct further work on the need for a deduction mechanism for internal TLAC, as proposed in guiding principle 10?***

HKAB agrees that a deduction mechanism should be established for internal TLAC in the form of non-regulatory capital instruments, to the extent that such mechanism is consistent with the corresponding deduction approach under the existing Basel III deduction mechanism for regulatory capital. In other words, the resolution entity should deduct from its non-regulatory capital TLAC resources if it holds internal TLAC of the same form issued by its material sub-group. This should ensure that the regulatory capital of the resolution entity is not affected by the internal TLAC arrangements.

For the avoidance of doubt, internal TLAC should not be characterised as external TLAC for the purpose of the "Tier 2 deduction approach" stipulated in the TLAC Holdings Standard issued by the Basel Committee on Banking Supervision on 12 October 2016. Hence by holding internal TLAC, the resolution entity should not be subject to Tier 2 capital deduction for the purpose of regulatory capital calculation on a solo basis.

Question 8: ***Do you agree with the obstacles to the implementation of internal TLAC mechanisms set out in guiding principle 12? How should G-SIBs and authorities address those obstacles and what additional obstacles, if any, might arise?***

Generally, HKAB agrees with the obstacles set out in Guiding Principle 12. In particular, HKAB supports the FSB's proposal to exclude internal TLAC instruments from the regulatory framework for large exposures. HKAB takes the view that all internal TLAC instruments should be excluded from any large exposure limits applied on an intra-group basis. The main purpose of holding internal TLAC is to upstream losses from the material sub-group to the resolution entity in support of its resolution strategy and this is inconsistent with the large exposure limit concept which aims to limit the potential losses from any single counterparty. HKAB would appreciate guidance from the FSB on some of the issues that are likely to be common to a number of jurisdictions to ensure consistency of approaches.

While TLAC instruments are subject to write-down and/or conversion into equity, unlike Additional Tier 1 and Tier 2 instruments, they are not regulatory capital securities and hence should be treated as debt instruments for tax purposes unless they are issued in the form of shares.

In addition to the obstacles outlined by the FSB, HKAB notes that it would be difficult to implement the internal TLAC mechanism in countries where there are capital controls or limitations on the transferability of liquidity, capital or funding.

HKAB notes that the conversion of internal TLAC could be problematic in relation to listed companies because shareholders' approval may be required. In the case of a resolution strategy where a listed company is a resolution entity and internal TLAC is issued to the listed company's holding company, this may constitute a connected transaction under the applicable stock exchange's listing rules and connected transactions rules would apply (e.g., this could trigger a requirement for shareholder approval, recommendations from an independent financial advisor, etc.).

HKAB suggests that the FSB discusses with resolution authorities the possibility of adopting statutory mechanisms to address this issue.

Question 9: ***Do you agree with the key features of contractual trigger language for internal TLAC, as set out in guiding principle 13 and in Annex 2? Should authorities consider the use of contractual triggers for internal TLAC in the form of regulatory capital instruments, including in cases where statutory point of non-viability powers exist in relation to such instruments?***

HKAB believes that (subject to the final principles for assessing recapitalisation needs for the subsidiary) the host authority should be responsible for determining the capital shortfall and recapitalisation level of a material sub-group that has reached the point of non-viability (***PONV***). If the required recapitalisation level is less than the total internal TLAC available, a partial write-down or conversion into equity of internal TLAC would occur.

HKAB requests the FSB to clarify how the partial write-down or conversion into equity would occur, i.e., whether (i) some tranches of internal TLAC would be written-down or converted whilst some tranches would be left intact; or (ii) all tranches of internal TLAC would be written-down or converted proportionally.

HKAB also believes that contractual write-down provisions may not be required where there is an adequate statutory regime that allows regulatory action, in the form of write-down or conversion, at the PONV as determined by the resolution authority.

In particular, HKAB would be grateful for further clarification from the FSB on the following issue: when a host authority has determined that the applicable material sub-group has reached PONV, is it the intention that (i) regulatory capital instruments (already having contractual PONV triggers in accordance with the Basel III requirements) and internal TLAC in the form of non-regulatory capital instruments would be written down and/or converted into equity at the same time; or (ii) there would be two scenarios of PONV - one for regulatory capital and another for TLAC?

Question 10: ***Do you agree with the process for triggering internal TLAC in Section V? In particular, what are your views on the timeframe for the home authority to decide whether to consent to the write-down and/or conversion into equity of internal TLAC?***

HKAB believes that the process of notifying the home authority is appropriate, however, there should be a parallel obligation to notify the board of the applicable resolution entity to ensure that appropriate actions are taken by the host authority and the company. We note that the write-down of internal TLAC would be disclosable and may therefore challenge subsequent recovery actions. Hence, it may be necessary to ensure that the 48-hour notice encompasses 48 business hours, as available recovery options may only be executed when banks and markets are open.

In order to avoid any unnecessary triggering of systemic effects, it is important that the home authority provides an affirmative consent to conversion of internal TLAC in order to materialise that there are no other possibilities to restore the level of capital of the material sub-group. HKAB's view is that an early triggering of TLAC with inconsistent disclosure to the market could have a devastating effect on the relevant bank and the market as a whole, including in the host country.

In respect of alternative pre-PONV options, HKAB requests that the applicable G-SIB is involved in all consultations with host and home authorities on any such potential options to restore the material sub-group's viability.

Question 11: ***Are there any other actions that should be taken by G-SIBs and authorities to support the implementation of the internal TLAC requirement, consistent with the TLAC term sheet?***

The final Guiding Principles must allow home authorities to take a proactive role to ensure that the implementation of internal TLAC requirements will be guided by coherent, group-wide views, respecting host authorities' needs and concerns, but also maintain consistency and effectiveness.

HKAB requests that the FSB ensures fair tax treatment (i.e., no unintended tax consequences) for implementation of the internal TLAC requirement.

Furthermore, HKAB would like the FSB to provide further clarity on the following:

(i) confirmation of the timeline to achieve the internal TLAC requirements; and

(ii) confirmation that any entity that does not form a part of a bank's material sub-group will not require internal TLAC and therefore will not be part of the computation of external TLAC requirement for the parent resolution entity.

Submission of The Hong Kong Association of Banks in response to

the Financial Stability Board's 16 December 2016 Consultative Document on

Guidance on Continuity of Access to Financial Market Infrastructures ("FMIs") for a Firm in Resolution

16 February 2017

Introduction

The Hong Kong Association of Banks (***HKAB***) was created by The Hong Kong Association of Banks Ordinance in 1981, which among other things provides a framework for the Hong Kong Government to exchange views with the banking sector for the further development of the industry. Every fully licensed bank operating in the Hong Kong Special Administrative Region must be a member of HKAB and subject to HKAB's rules. The roles of HKAB include being a focal point for consultation on law reform, new legislation and regulatory matters.

HKAB has reviewed the Consultative Document on Guidance on Continuity of Access to Financial Market Infrastructures (***FMIs***) for a Firm in Resolution (the ***Consultative Document***) and received feedback from members of HKAB on the Consultative Document. This paper, which was prepared with the assistance of international law firm Freshfields Bruckhaus Deringer, sets out the views of HKAB based on the feedback it has received from HKAB members.

Questions from the Consultative Document on which HKAB is providing its views are repeated below in bold italics, with HKAB's views set forth following each question.

General Comments

HKAB's members include FMI intermediaries (i.e., firms that provide clearing, payment, securities settlement and/or custody services to other firms and that are direct members of one or more FMIs), FMI participants (i.e., firms with direct access to FMI services – e.g., through being a direct member of an FMI – or with indirect access to an FMI through an FMI intermediary) and Providers of critical FMI services (e.g., custodians or FMI intermediaries that provide critical FMI services), in each case as those terms are defined in the Consultative Document).

Responses to Consultation Questions

Question 1: ***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?***

Some of the proposals will require entities that are not in resolution (particularly FMI intermediaries and providers of critical FMI services) to take steps to ensure continued access to FMIs by other firms that are in resolution. HKAB understands why these requirements are appropriate as a policy matter. However, if there are any extra indirect or direct financial costs that arise when a firm (that is not in resolution) complies with these requirements (i.e., provides a firm in resolution with continued access to an FMI) then the firm (that is not in resolution) should be compensated for all of those extra costs.

Banks that are FMI intermediaries will need to assess the commercial impact of additional liquidity requirements prescribed by FMIs for continued access in resolution. Where a bank acts as an FMI intermediary, any additional liquidity requirements will similarly apply to their clients and may result in increased costs of clearing.

Question 2: ***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.***

HKAB is very supportive of the proposition that continuity of access to FMIs through resolution is a point that needs to be addressed in order for authorities and market participants to have confidence that resolution strategies and plans can be implemented in practice. Further, HKAB in general agrees that the proposals in the Consultative Document are appropriate arrangements for supporting continued access to FMIs by a firm in resolution.

HKAB notes that SWIFT provides secured financial messaging with FMIs which is not currently substitutable. As SWIFT is a co-operative, individual participants cannot bilaterally negotiate terms of access. We urge that this dependency be addressed in the consultation conclusions.

For clarity, it would be helpful for the FSB to further clarify the meaning of "FMI participant" and "firm" (i.e., whether these terms include only those entities that are systemically important).

Question 3: ***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?***

At present most central counterparties (***CCPs***) can close out a clearing member before an actual insolvency (e.g., close out may be permitted due to unpaid margins, default of an affiliate, default at another FMI, etc.). FMI rules are usually written to give a CCP discretion as to when to close out a member.

Given the systemic importance of clearing generally and the criticality of firms having access to derivative markets and derivatives clearing, HKAB believes that it is essential for a bank in (or leading to) resolution to continue to have access to the key FMIs. This requires the CCP rules to reduce the extent of discretion and to allow a bank in resolution to keep being a member, as long as the member keeps paying margin. This can be seen as a quid-pro-quo for the fact that resolution is designed to avoid the default management process at the FMI, therefore reducing risk to the FMI.

In Hong Kong, certain important clearing and settlement systems that are owned or operated by the Hong Kong Government are out of scope from Hong Kong's statutory resolution regime. HKAB assumes that in at least some other jurisdictions there will also be important clearing and settlement systems that are outside of the scope of the local resolution regime. We envision that it could be critical in resolution for a firm to have continued access to a particular clearing and settlement system regardless of whether or not that system is within the scope of the local resolution regime, and suggest that the consultation conclusions should include a statement to the effect that the guidance applies to access to all FMIs, whether or not the particular FMIs are within the scope of their local resolution regimes.

For state controlled FMIs, central banks and resolution authorities should collectively transition membership rules to accommodate continued access in resolution where participants are solvent. We refer to the recent revisions to CHAPS membership rules.

For privately owned FMIs, contractual arrangements should be revised and standardised through collaboration between the FMI, participants and central banks.

Question 4: ***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.***

See response to Question 1 above. Where a provider of critical FMI services does not exercise a right of termination or suspension and continues to provide access to critical FMI services to another firm that is in resolution, it is important not only that the firm in resolution continues to meet its payment, delivery and collateral provision obligations but also that any extra direct or indirect costs to the provider of critical FMI services are compensated. For example, if under capital requirements applicable to the provider of critical FMI services there are increased costs due to the firm continuing to provide services to the other firm in resolution those increased costs should be compensated.

In addition, HKAB agrees that in general continued access for a limited period of time is likely to be beneficial for the wider sector and so should be supported. Many FMIs, particularly CCPs, will increase margin considerably if credit quality of a member firm worsens. This is helpful in incentivising firms to reduce risk. However, this should not be so extreme as to make it difficult for the firm in trouble to manage its risk. FMIs should clearly set out in their rules not only how they deal with a firm in resolution, but also what additional margin and other steps they will require and how they deal with such a firm in the run-up to resolution.

Question 5: ***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 an 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?***

HKAB agrees that such general rights, arrangements and applicable procedures of a provider of critical FMI services should be the same irrespective of whether the firm entering into resolution is a domestic or foreign FMI participant.

Question 6: ***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?***

It could be practically challenging for some providers of critical FMI services (which includes custodians) to engage with participants on a bilateral basis in respect of the "*range of risk management actions and requirements they would anticipate taking in response to the resolution of an FMI participant*". Instead HKAB would expect providers to set out a position that could be made publicly available to participants / prospective participants.

In addition, in some circumstances it would be appropriate for this engagement to be achieved through working groups rather than bilaterally.

Question 7: ***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?***

HKAB notes that liquidity contingency plans and Recovery Plans are already in place, and notes that it could be difficult and not particularly meaningful to develop a detailed contingency plan for access to various FMIs on top of this. A high level playbook on liquidity sources would be more appropriate.

A practical approach would be to retain existing FMI providers upon entry into resolution under the measures and scenarios described in Section 1.3 of the Consultative Document (i.e., additional collateral, margin, contribution to guarantee funds, etc.). Standby contingency options may not be effective as alternative providers may follow the lead of the primary FMI provider in the absence of additional information.

Question 8: ***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.***

HKAB's view is that the situation is different for brokers providing access to an FMI to other firms, especially if the FMI is a CCP. The CCP has a deep default management waterfall, enabling it to not only call margin, but to rely on mutualised resources to deal with a member default, namely the default fund and assessments. A broker only has margin to deal with in the event of the default of a client. Some of this margin has been reduced with recent changes on how client margin for futures is to be treated.

There is a trade-off between more rigid rules to avoid cutting firms off from derivatives markets and the lower likelihood of a default by the client entering into resolution.

To protect the capital of the broker, there should be more leeway for brokers to increase margin requirements to protect themselves in the run-up to a resolution. Again there should be clear requirements on how this is to be done, and to what extent the firm nearing resolution should reduce its risk.

Question 9: ***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?***

HKAB has no comments beyond the responses it has provided elsewhere in this letter.

Question 10: ***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?***

HKAB requests further guidance on protocols to ensure a participant in resolution will continue to receive funds on an intra-day basis owed to it by other participants. Delayed receipts may affect its ability to clear.