



BANK FOR INTERNATIONAL SETTLEMENTS

Principles for Financial Market Infrastructures (PFMIs), Disclosure Framework & Assessment Methodology

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Windhoek, October 2017

* Views expressed are those of the author and not necessarily the views of the BIS





Introduction to PFMI



Organisation of the PFMI



Highlights and challenges



Assessment Methodology



Disclosure Framework



Why PFMIIs?

Support financial stability

- Payment and securities settlement systems worldwide support financial system stability

LVPS

- The 2008 financial crisis showed that the domestic (e.g. RTGS systems) and global (e.g. CLS Bank) payment infrastructure was able to withstand the financial storm, and was instrumental in facilitating immediate responses by authorities.

Systems are increasingly interconnected

- Securities settlement systems are increasingly interlinked to funds transfer systems and operate under a DVP arrangement. These are crucial for the development of capital markets, and for the timely delivery of collateral for payments and other purposes

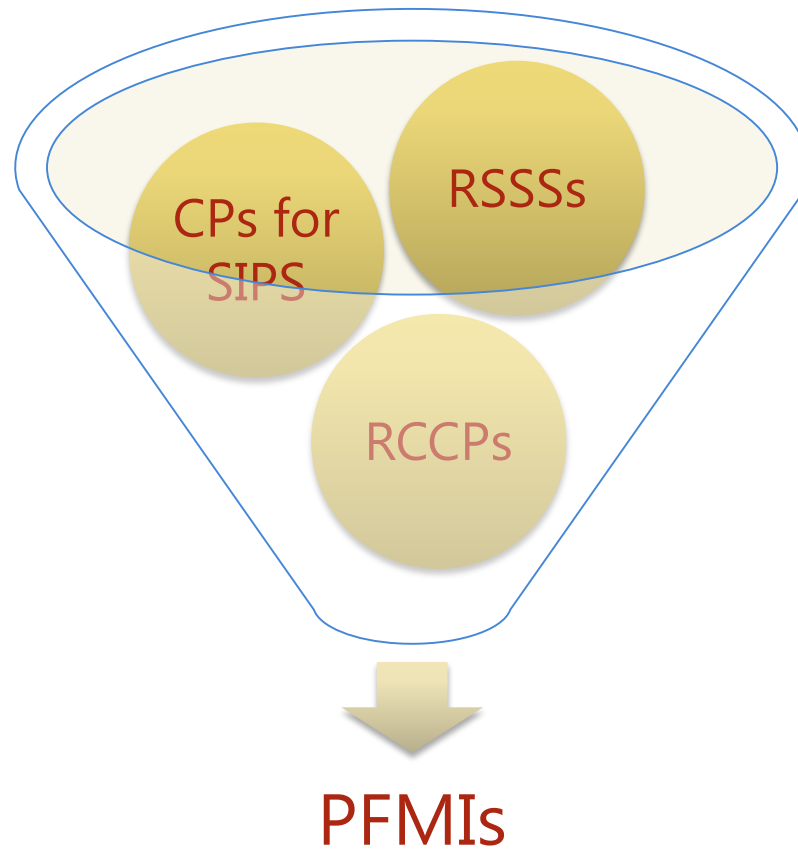
OTC derivatives can create systemic risk

- Significant counterparty credit risk in OTC derivatives markets
- Shortcomings in default and liquidity risk management
- Severe lack of transparency in the OTC derivatives markets and absence of infrastructure to mitigate risk
- September 2009 G20 Pittsburgh Summit, June 2010 G20 Toronto Summit Declaration, Annex II - central clearing in CCPs and reporting all OTC contracts to TRs.

Supports G20 and FSB goals

- ...to strengthen financial infrastructures and financial markets by strengthening existing standards

PFMIs - a single set of standards



CPSS-IOSCO Report on Principles for FMIs, 2012

- Applicable to payment systems (PSs) of systemic importance, CSDs, SSSs, CCPs, and TRs
- Strengthens and harmonises previous international standards
- Strengthens responsibilities of relevant regulatory authorities in regulating, supervising, and overseeing FMIs
- “Raising the bar”: more-demanding requirements and greater guidance compared with previous standards
- Functional approach to the applicability of the principles
- Applies to both public sector and private FMIs that are systemically important

Raising the bar

Increased complexity

- Financial markets are more complex

New topics

- New FMI: Trade repository (TR)
- General business risk, tiered participation, collateral
- These topics already existed in the previous standard, however not as individual principles
- Clear distinction between CSD and SSS

Higher requirements

- Operational risk management, governance, liquidity risk, credit risk, among others

Highlights the importance of a comprehensive view of risk management

- Participant and its affiliates
- Risks that an FMI poses to and bears from other FMIs (Interdependencies)
- Recovery and resolution of FMIs (CPSS-IOSCO report)

Raising the bar (continues)

Strengthened credit risk standards

- Full coverage of a PS or SSS's current and potential future exposures to each participant with a high degree of confidence
- Cover 2 for a DNS or SSS without settlement guarantee

Strengthened liquidity risk standards

- Maintain sufficient liquid resources to effect same day (intraday, where appropriate) settlement of payment obligations in all relevant currencies
- Withstand the default of the participant and its affiliates with the largest liquidity obligation
- Replenish liquidity resources following a stress event

For both credit and liquidity risk

- Regularly test the sufficiency of FMI's resources (stress testing)
- Explicit rules and procedures to address uncovered shortfalls from a participant's default

Other aspects

- Stronger emphases on business continuity, transparency (disclosing more information), encourage direct access, links, governance

Comprehensive framework for management of risks

FMI's risk-management framework includes its authority, structure, rights, and responsibilities

- the legal basis for the FMI's activities (PFMI1)
- the governance structure of the FMI (PFMI2)
- the framework for the comprehensive management of risks, to help establish a strong foundation for the risk management of an FMI (PFMI3)
- PFMI1s are designed to ensure that the infrastructure supporting global financial markets is more robust and thus well placed to withstand financial shocks
- An FMI should have a sound risk-management framework for comprehensively managing legal, credit, liquidity, operational, and other risks.

Use of PFMI

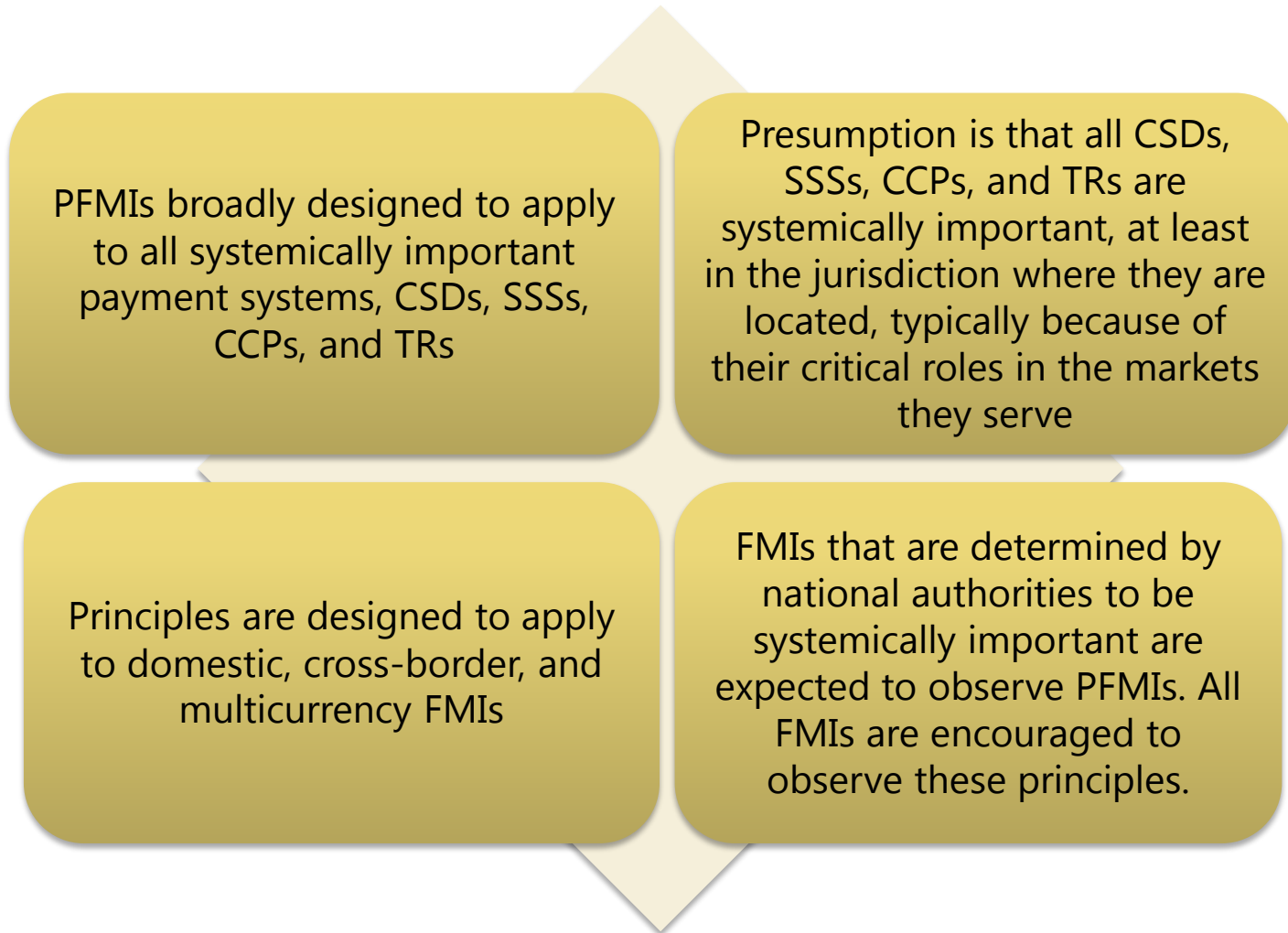
By FMIs: FMIs to conduct formal periodic full/partial self-assessments, where this is consistent with national practice.

By authorities (overseers): As part of their regulation/oversight Responsibilities, national authorities are expected to regularly assess observance of the Principles by FMIs. Authorities are also encouraged to conduct periodic self-assessments of their observance of the Responsibilities.

By IMF and WB): CPSS and IOSCO are encouraging external assessments of FMI observance of the Principles and authorities' observance of the Responsibilities, including assessments conducted by IMF and WB, in particular as part of FSAP.

Common goal among all assessors is to determine whether and how well an FMI observes the principles or an authority fulfills the responsibilities.

PFMIs Scope



What is an FMI?

- FMI is defined as a multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions.
- A set of common rules and procedures for all participants, centralised clearing, settlement, and recording of financial transactions, a technical infrastructure, and a specialised risk-management framework
- Some FMIs are critical to helping central banks conduct monetary policy and maintain financial stability

FMI's can differ significantly in organisation, function and design

- Organisation: a variety of forms, including associations of financial institutions, non-bank clearing corporations, specialised banking organisations
- May be owned and operated by a central bank or by the private sector
- May operate as for-profit or not-for-profit entities
- Depending on organisational form, FMIs can be subject to different licensing and regulatory schemes within and across jurisdictions
- Significant variations in design among FMIs with the same function

Organization of PFMI

General organization	• PFMI 1, 2, 3
Credit and liquidity risk management	• PFMI 4, 5, 6, 7
Settlement	• PFMI 8, 9, 10
CSDs and exchange-of-value system	• PFMI 11, 12
Default management	• PFMI 13, 14
General business and ops risk	• PFMI 15, 16, 17
Access	• PFMI 18, 19
Efficiency	• PFMI 21, 22
Transparency	• PFMI 23, 24

Principle	CPSIPs	RSSSs	RCCPs
1. Legal basis	1	1	1
2. Governance	10	13	13
3. Framework for the comprehensive management of risks	3	-	-
4. Credit risk	3, 5	9	3, 5
5. Collateral	5	9	4, 5
6. Margin	-	-	4, 5
7. Liquidity risk	3, 5	9	5
8. Settlement finality	4	8	-
9. Money settlements	6	10	9
10. Physical deliveries	-	-	10
11. Central securities depositories	-	6, 11, 12	-
12. Exchange-of-value settlement systems	-	7	10
13. Participant-default rules and procedures	-	-	6
14. Segregation and portability	-	12	-
15. General business risk	-	-	-
16. Custody and investment risk	-	12	7
17. Operational risk	7	11	8
18. Access and participation requirements	9	14	2
19. Tiered participation arrangements	-	-	-
20. FMI links	-	19	11
21. Efficiency and effectiveness	8	15	12
22. Communication procedures and standards	-	16	-
23. Disclosure of rules, key procedures, and market data	2	17	14
24. Disclosure of market data by trade repositories	-	-	-

Principle	PSs	CSDs	SSSs	CCPs	TRs
1. Legal basis	●	●	●	●	●
2. Governance	●	●	●	●	●
3. Framework for the comprehensive management of risks	●	●	●	●	●
4. Credit risk	●		●	●	
5. Collateral	●		●	●	
6. Margin				●	
7. Liquidity risk	●		●	●	
8. Settlement finality	●		●	●	
9. Money settlements	●		●	●	
10. Physical deliveries		●	●	●	
11. Central securities depositories		●			
12. Exchange-of-value settlement systems	●		●	●	
13. Participant-default rules and procedures	●	●	●	●	
14. Segregation and portability				●	
15. General business risk	●	●	●	●	●
16. Custody and investment risk	●	●	●	●	
17. Operational risk	●	●	●	●	●
18. Access and participation requirements	●	●	●	●	●
19. Tiered participation arrangements	●	●	●	●	●
20. FMI links		●	●	●	●
21. Efficiency and effectiveness	●	●	●	●	●
22. Communication procedures and standards	●	●	●	●	●
23. Disclosure of rules, key procedures, and market data	●	●	●	●	●
24. Disclosure of market data by trade repositories					●

PFMIs: Responsibilities for Authorities

Responsibility A: Regulation, supervision, and oversight of FMIs	FMIs should be subject to appropriate and effective regulation, supervision, and oversight by a central bank, market regulator, or other relevant authority
Responsibility B: Regulatory, supervisory, and oversight powers and resources	Central banks, market regulators, and other relevant authorities should have the powers and resources to carry out effectively their responsibilities in regulating, supervising, and overseeing FMIs
Responsibility C: Disclosure of policies with respect to FMIs	Central banks, market regulators, and other relevant authorities should clearly define and disclose their regulatory, supervisory, and oversight policies with respect to FMIs
Responsibility D: Application of the principles for FMIs	Central banks, market regulators, and other relevant authorities should adopt the CPSS-IOSCO Principles for financial market infrastructures and apply them consistently
Responsibility E: Cooperation with other authorities	Central banks, market regulators, and other relevant authorities should cooperate with each other, both domestically and internationally, as appropriate, in promoting the safety and efficiency of FMIs

Responsibilities of Authorities: mapping against the previous framework

Responsibility	CPSIPSs	RSSSs	RCCPs
Responsibility A. Regulation, supervision, and oversight of FMIs	A	18	15
Responsibility B. Regulatory, supervisory, and oversight powers and resources	C	18	15
Responsibility C. Disclosure of objectives and policies	A	18	15
Responsibility D. Application of the principles for FMIs	B, C	-	-
Responsibility E. Cooperation with other authorities	D	18	15

Additional documents/report

- CPMI-IOSCO: Guidance note “Application of the Principles for financial market infrastructures to central bank FMIs, 2015
- CPMI-IOSCO: Recovery of Financial Market Infrastructures, 2014 (revision 2017)
- CPMI-IOSCO: Principles for FMIs: Assessment Methodology for the Oversight Expectations Applicable to Critical Service Providers, 2014
- CPSS-IOSCO: OTC derivatives data reporting and aggregation requirements; Public quantitative disclosures, 2014
- CPMI-IOSCO: Guidance on Cyber Resilience in FMIs, 2016
- Resilience of central counterparties (CCPs): Further guidance on the PFMI, 2017

Assessment Methodology

CPSS-IOSCO report on Disclosure Framework & Assessment Methodology, 2012

- The report on DF&AM is complementary to the Report on Principles for FMIs

Provides guidance for assessing observance of the 24 principles and 5 responsibilities.

- Practical guidance regarding the scope of an assessment, data gathering, developing key conclusions and recommendations, rating the observance for each principle, and assigning appropriate timeframe to addressing key recommendations

Each principle contains Key Considerations complemented by Key Questions

Intended to promote objectivity and comparability across the assessments of observance in different countries

Assessments should be conducted regularly and disclosed

Who can use the Assessment Methodology?

Intended primarily for external assessors, such as WB and IMF

- FSAP framework and in technical assistance programmes

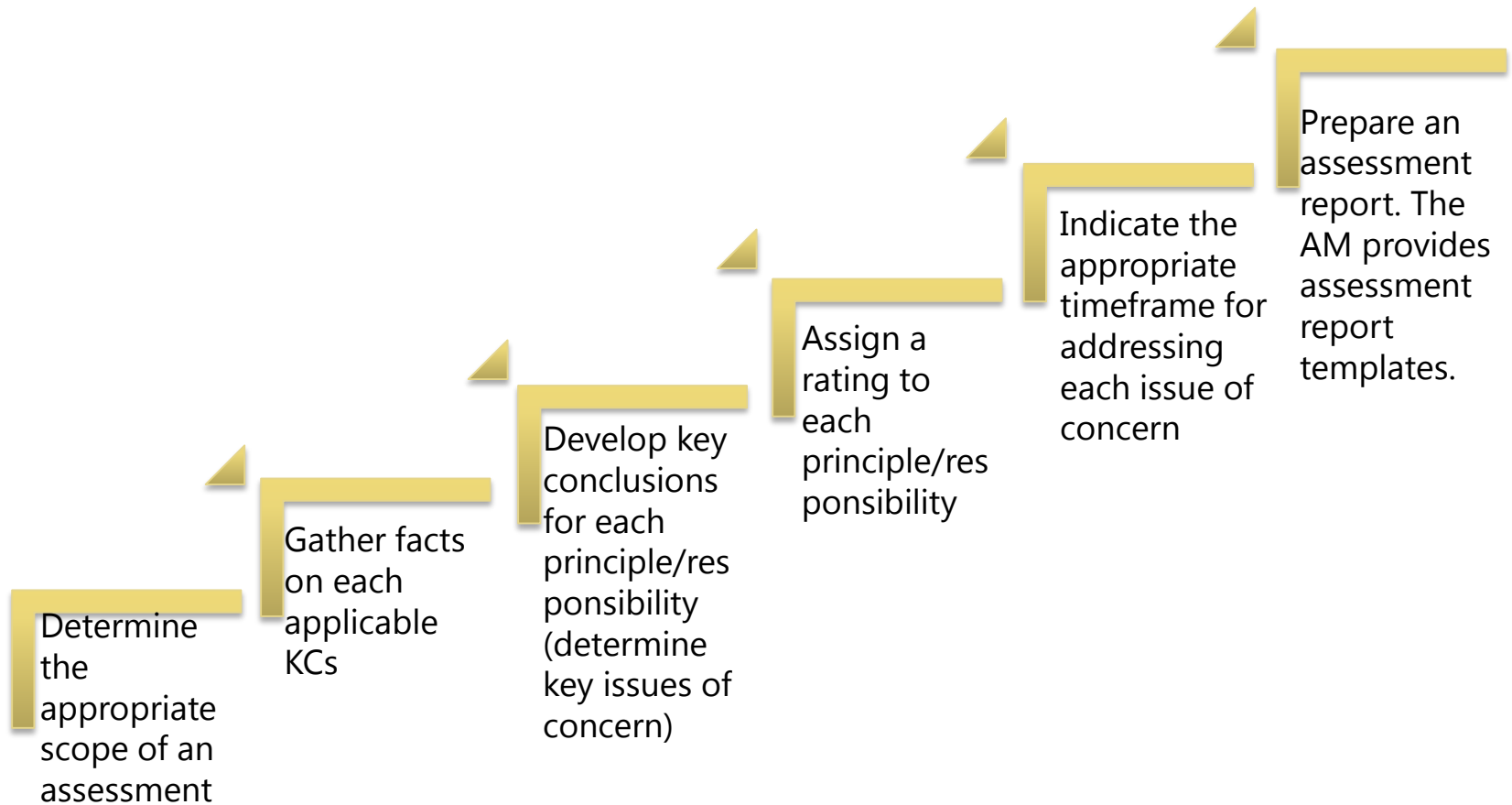
By central banks and other authorities at the national level to conduct assessments in their capacity as overseer (or self-assessments as operators) of FMIs

- For regular or ad-hoc assessments

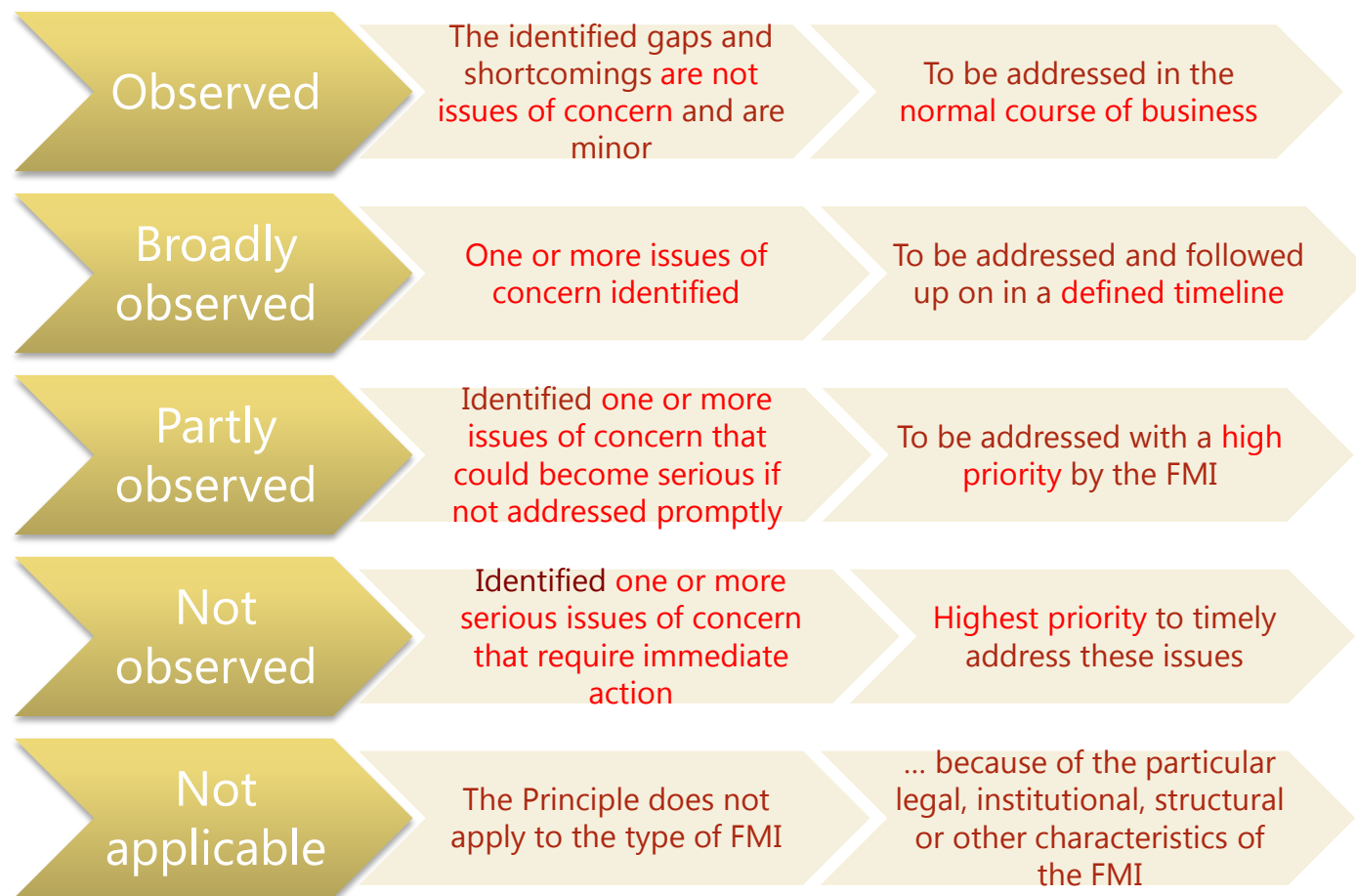
AM an useful tool for an FMI in its decision-making process

- To conduct formal periodic full or partial self-assessments of observance of the principles
- When introducing new products or services or major changes to its policies, rules or procedures

Six steps involved in an assessment of PFMI's observance



Ratings



Use of a rating framework

WB/IMF use the rating scheme presented in the AM in the context of the FSAP

- **National authorities** may use the AM rating framework or another rating framework
- in particular when it is legally bound to use a different AM
- if different rating framework, that framework should be as effective as the AM rating framework for assessing FMIs
- AM rating framework to be used in the context of cross-border cooperative oversight arrangements unless agreed otherwise

Where consistent with national practice, **FMI**s should use the AM rating scheme

Assessment report template: Rating summary on the observance of the PFMI

Table: Ratings Summary of the Principles for the	
Assessment category	Principle
Observed	Principles ...
Broadly observed	Principles ...
Partly observed	Principles
Not observed	Principles
Not applicable	Principles

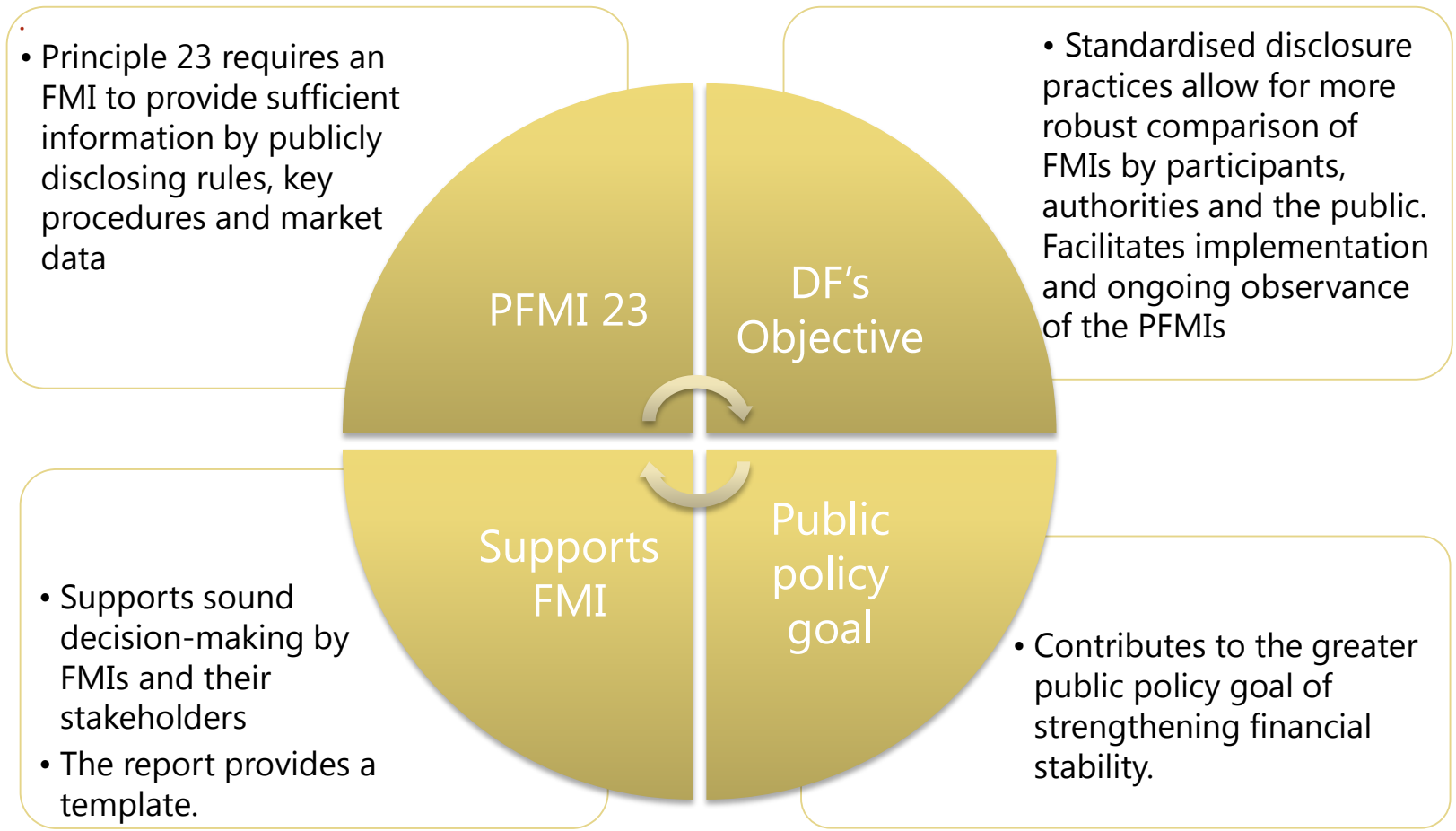
Assessment report template: Recommendations

List of Prioritized Recommendations for Principles				
Principle	Issues of Concern and Other Gaps or Shortcomings	Recommended Action	Relevant Parties	Comments and Priority
1	...	...	...	...
2				

Disclosure framework ↔ Assessment methodology

- CPMI-IOSCO Report on DF & AM, 2012
- The DF uses the questions that have been developed for the AM to ensure comprehensive disclosure of the FMI's risks and risk management and other practices
- The AM uses the DF as one of the key sources of information for the assessment of observance of the PFMIIs.
- The DF also supports the AM by providing assessors with a basic set of facts from which to begin their assessments of FMIs

Disclosure Framework



Thank you

www.bis.org/cpmi

