

PUBLIC SELF ASSESSMENT

20th August 2017

2017 CHAPS Co FMI disclosure report amendment

Responding institution: CHAPS Co Clearing Company Limited

Jurisdiction(s) in which the FMI operates: United Kingdom (with international participants operating through branch locations within the United Kingdom)

Authority(ies) regulating, supervising or overseeing the FMI:

1. Recognised by HM Treasury as an inter-bank payment system under Part 5, §185 of the Banking Act 2009.
2. Supervised by the Bank of England pursuant to The Banking Act 2009 and designated as a "system" by the Bank of England, as the relevant designating authority under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (the "SFRs"), which implement the EU Settlement Finality Directive 98/26/EC in the United Kingdom.
3. Supervised by the Payment Systems Regulator pursuant to the Financial Services (Banking Reform) Act 2013 which came into force on the 1st April, 2015.

The date of this disclosure is **20th August 2017 and is an amendment to the original disclosure 28th April 2017**¹. Additionally, the Company may, from time to time, amend this disclosure as necessary to ensure that any significant or material developments are accurately noted.

This document can also be accessed online at:

http://www.chapsco.co.uk/files/chaps/chaps_cpss_iosco_summary_report_final.pdf

I. Executive summary

The CHAPS Clearing Company Limited ('The Company' or 'CHAPS Co') has its registered offices at 2 Thomas More Square, London, E1W 1YN. The Company is responsible for the facilitation of participation in the CHAPS payment system and is wholly owned by its Participants, who, as Members of the Company, each hold a .10p share and contribute to the operational running costs of CHAPS Co Clearing Company Limited. Scheme Participants are authorised credit institutions and a current list of Scheme participants can be found on the company's website at:

<http://www.chapsco.co.uk/access/current-participants>

As noted above, the CHAPS payment system is recognised by HM Treasury as a *recognised* payment system and has also received designation from the Bank of England. As at 1st April 2015, it is also supervised by the Payment Systems Regulator. The Company has a Board of 16 Directors headed by an Independent Chairman with four other Independent Directors also appointed to the Board. The Bank of England is represented by an appointed observer rather than a Director to avoid any conflicts of interest as the regulatory overseer. There are no executive directors.

¹ Subsequent to the completion of CHAPS Co's 2017 self-assessment against the CPMI-IOSCO PFMI, the Bank of England announced on 9 May 2017 that it would take over the operation of the CHAPS payment system under a direct delivery model. This is not covered within the scope of this assessment.

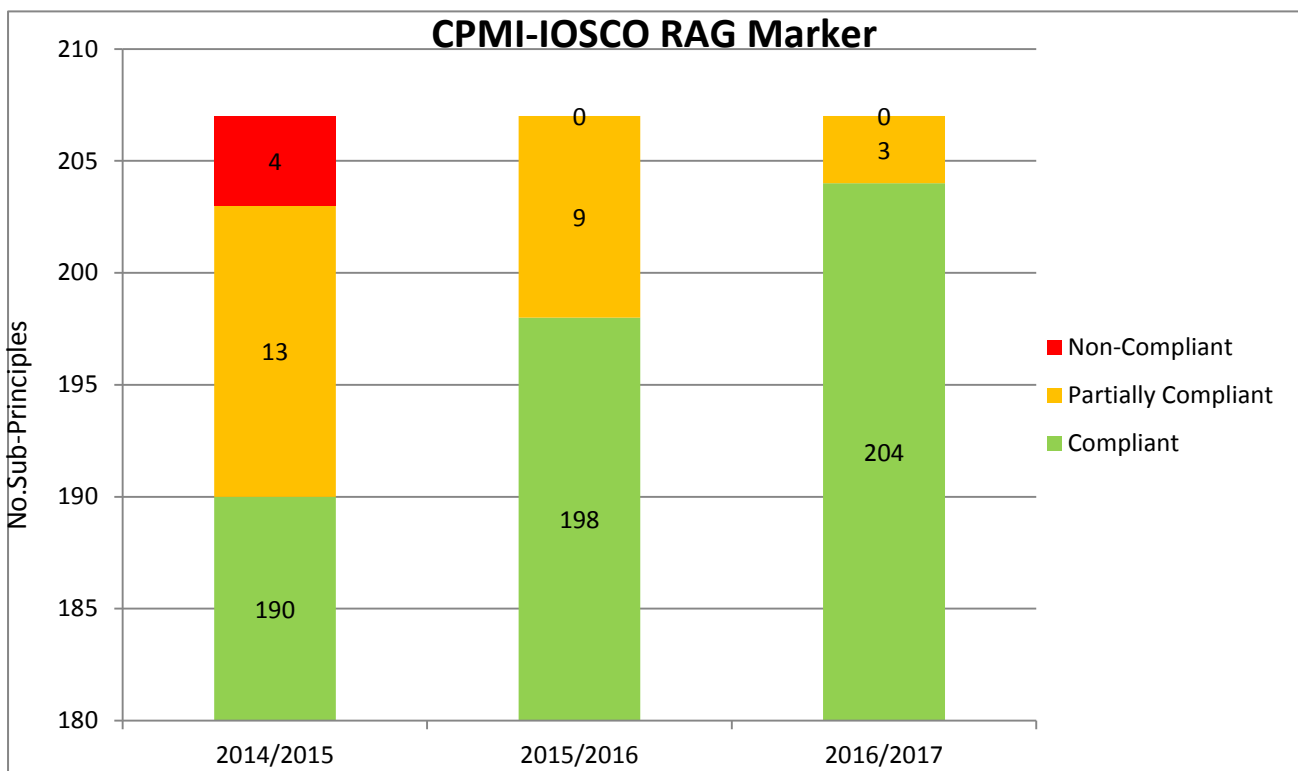
The Memorandum and Articles of the Company² set out the conduct of Board Meetings. During this period the Company has undergone significant Governance restructure during this period to ensure that the Board remains 'fit for purpose' and that structure governance processes are appropriate for current and future activity.

The Company is a private company limited by shares and is responsible for the facilitation of participation in the CHAPS payment system which provides real time gross settlement for sterling payments in the UK. To this end, the Company, as facilitator of a critical financial market infrastructure and pursuant to its designation by the Bank of England as a systemically important financial market infrastructure, and its Board of Directors are responsible for ensuring the mitigation and management of systemic risk as well as supporting any PSR objectives in relation to access and innovation. This includes the setting of appropriate and transparent participation rules and procedures, managing services provided to participants, responding to any PSR and BoE directions and market reviews as appropriate, monitoring payment system risks and participants' compliance to the rules and requirements and generally managing operational and strategic development of the Company and its payment settlement activities. The Company does not provide any other services.

CHAPS Co has undertaken a "long form" assessment against all applicable Principles, considerations and questions set out in the CPMI/IOSCO Disclosure Framework and has assessed itself in detail against the 16 principles that are relevant to itself. The long form assessment is provided, with this covering report, to the Bank of England, the CHAPS Co Board and the CHAPS Risk and Governance and Discipline Committees.

In contrast to last year's self-assessment which identified a number of gaps where CHAPS Co could only show partial compliance (marked with a AMBER RAG status), this year's self-assessment not only shows that there are no RED RAG markers, but additionally, there are also significantly fewer AMBER markers (i.e. areas where there may be only partial compliance). As in preceding years, the Company has created a separate CPMI IOSCO tracker which subsequently addresses any identified gaps via an agreed action plan.

The table below shows the comparison between the Company's self-assessment last year and this year and illustrates an overall compliance increase of 3%.



² See the Company's Key Governance Documentation at <http://www.chapsco.co.uk/governance/key-documentation>

A more detailed table showing the breakdown between compliant and partially compliant markers can be found at paragraph IV of this report.

II. Summary of major changes since the last update of the disclosure

This is the fifth time that CHAPS Co has self-assessed itself against the relevant CPMI principles since its introduction in December 2012 and for 2017 CHAPS Co has also self-assessed against the CPMI Cyber compliance annex. The Board approved CHAPS Co strategic plan 2013-17 forms the basis of the strategic direction over the period. The strategic deployment is an active process, overseen by Board and executed by the Executive Management Team. Over the period the strategy has evolved in the light of changing significant internal and external events. In the period the Board has revalidated the strategic vision, reconfirmed strategic purpose and reassessed strategic priorities. This has resulted in the strengthening of the governance/reporting/monitoring processes to ensure strategic priorities are executed effectively in a risk focused manner and for the strategic framework against which CHAPS Co monitors critical strategic deliverables. The five core priorities are:

- Effective Governance
- Operational Excellence
- Robust Risk Management
- Fair and Transparent Access
- System Innovation

Underpinning these priorities are 73 'Signature Actions' and good progress continues to be made against these actions. In 2017 a further 8 signature actions have been identified to ensure strategic focus is maintained.

An overview of significant changes arising since the Company's April 2016 self-assessment is as follows:

Board and Governance

- Implemented proposals to restructure the Board and Committees which included 2 further Independent Non-Executive Directors appointed by September 2016 bringing total of Independent Directors to 5 and the revised 16 member Board Composition was effective October 2016.
- Board member appointments are now controlled by an enhanced set of guidelines which includes a comprehensive competency assessment. The overall competency/diversity of the Board is managed through a dashboard process. Competency updates are required periodically and training needs are assessed as part of this process. The next external Board effectiveness review will take place in Q1 2018.
- From 2017 the existing quarterly board meeting structure has been supplemented by two additional thematic Board meetings, focusing respectively on major risk matters/horizon scanning (held in March 2017) and strategic business assessment and development (scheduled for September 2017) respectively.
- An amended Committee Structure was approved by Board (terms of reference) and implemented December 2016 (effective 1 January 2017) and the following changes were made to enhance governance effectiveness:
 - The Audit and Finance Committee ceased to exist as a separate committee;
 - The Governance and Compliance Committee took on responsibility for internal and external audit matters and became the Governance, Compliance and Audit Committee;

- The Business and Strategy Committee assumed responsibility for finance and became the Strategy and Finance Committee;
 - The Security Committee became directly accountable to the Board;
 - The Technical and Operations Committee became an executive Committee representing all Direct Participants. Its primary purpose remains to ensure the required availability and proper performance of the CHAPS System and indirectly, the extended operation of Direct Participants.
- Committee member competencies review exercise was initiated in Q1 2017 and is scheduled to be completed by end of Q2 2017.
 - Training for committee members ‘Making the most of Committees’ who were not Board members was carried out in October 2016 and Board members also received competition law training in February 2017.
 - To reflect the need for continued engagement at a strategic level a “shareholder representative” structure has been established. Each Direct Participant provides a shareholder representative to act as a senior conduit (independent of any Board members) for matters related to shareholder engagement.

Risk

- Developed and in the process of implementing an enhanced Direct Participant compliance and assurance process aligned with the launch of the new CHAPS Reference Manual in February 2017. The enhanced Participant Assurance approach uses self-attestation, questionnaires, data analysis and compliance testing to provide a more dynamic, granular and forward looking assessment of the systemic risks brought to the Scheme by its Participants.
- Implemented a standardized approach to Supplier and Third Party risk assessment based on the CPMI standards for Critical Service Providers.
- As one of the key recommendations of the PA Consulting ‘Outsourced Service Excellence’ report, implemented a Joint Risk Forum with risk and operations management from Bank of England RTGS to review shared and emerging risks, undertake stress and scenario planning and review risk mitigation and post-incident learnings.
- Implemented an emerging risk and horizon scanning process to identify and assess new risks in a structured manner.
- Enhanced the CHAPS Recovery Plan to align with CPMI guidance on Recovery of FMIs, including identification of early warning indicators, potential viability challenging scenarios, possible mitigating actions and agreement of a governance framework to oversee the recovery process.
- Undertaking a range of stress and scenario testing, focusing on both idiosyncratic and market wide events and assessing the quantitative and qualitative impacts on the Company and Scheme.
- Revised the intraday Throughput Criteria to take into account the Extended CHAPS Day and better link the targets and measurement points to the liquidity and operational risks that may arise.

Legal & Regulatory Affairs

- Re-execution of the CHAPS Participation Agreement (January 2017) by all existing Participants prior to adoption date of CHAPS Reference Manual.

- Adoption of CHAPS Reference Manual (February 2017).
- Restructuring of the Legal and Regulatory unit to move regulatory compliance to the Risk function, allowing the Legal and Regulatory Unit to focus on regulatory strategy and horizon scanning activities and provide independent legal advice to regulatory compliance function owned by Risk (February 2017).
- Completion and execution of the UK Payments Framework Services Agreement and Accommodation Licence (March 2017).

Business and Operations

- CHAPS continues to grow with two further Direct Participant banks on-boarding during 2016. Enhanced on-boarding processes, methods and controls have also supported the further significant growth of Onboarding in 2017/18 with a further 13 potential on-boarders being lined up (at this point 8 are locked in) whilst enabling CHAPS Co to continue to focus on the core objective of financial stability through thorough robust risk management, participant assurance and operational oversight.
- Industry standard based Incident and Problem Management processes have been fully embedded enabling even more robust incident handling, root cause analysis and common learning to drive down risk through shared learnings. This includes enhanced protocols, pre-planned communications, interfaces to key parties such as BoE, playbooks and major incident procedure enhancements. Implementation of a fully automated push messaging system, providing a more efficient and single point of entry mechanism for managing simultaneous multiple email, SMS and Voiceblast communications in the event of a live CHAPS incident was successfully implemented both useful for current and also as CHAPS expands over the next 24 months.
- Further scenario and stress tests have been undertaken including industry wide SIMEX testing allowing the execution of agreed crisis management procedures with relevant parties. This is part of an annual plan to continually challenge our ability to respond and react to relevant issues. There is a continual rolling plan of stress tests executed across the teams within CHAPS Co.
- As the global security challenges continue to evolve the CHAPS Co Security Roadmap was successfully delivered utilising industry standard models, including NIST, to further enhance the security capability. Multiple audits have validated the activities undertaken and where relevant any gap closures are planned and implemented/underway. In light of the demanding Cyber challenges a refresh of the strategy is underway to ensure appropriateness.
- Enhanced contingency requirements have been implemented across the Direct Participant community such as enforcing Tertiary Contingency for a sub set of our Direct Participants. In addition clarifications over the Disaster Recovery and Business continuity objectives have been made. These are within a major rebuild of the CHAPS Reference Manual which details our Rules, Requirements and Procedures used to ensure appropriate risk management across the CHAPS eco-system.
- In April 2016 CHAPS Co developed and implemented an enhanced framework for management of change/projects proportionate to the risk involved ensuring both efficiency and effectiveness whilst delivering controlled, sustainable and quality changes. This was used to deliver both BAU activities and the Signature Actions underpinning the delivery of the CHAPS Strategy.
- Significant governance enhancements with our core partners including BoE RTGS and SWIFT have driven collaboration across Change, On-boarding, Risk and Operations with assurance processes in place utilising various data feeds as well as ISAE3402, PFMI and relevant security

accreditation. This further drives our efficiency and effectiveness achieved through collaboration as we drive to further de-risk financial stability.

- To further drive resiliency across the scheme following the implementation of the revised CHAPS Manual (February) CHAPS Co has established dedicated functions aligned to driving participant performance. This utilises an industry leading assurance approach along with dynamic day to day metrics ascertained through operations and self-declaration from DPs all applied to a dynamic scorecard enabling bespoke, targeted, focused assurance questions to understand risk across the eco-system.

Further detail behind these key changes may be found at paragraph IV of this report.

III. General background on the FMI

General description of the FMI and the markets it serves

The CHAPS Clearing Scheme (the "Scheme") provides real time gross settlement for sterling payments in the UK. During the month of March 2017, the Scheme processed on average 159,235 electronic payments per day with a total value of £317 billion on average each day. A rolling twelve month view of CHAPS volume and values data can be found on the CHAPS website at:

<http://www.chapsco.co.uk/about-chaps/chaps-statistics>

The Scheme is currently operated by CHAPS Clearing Company Limited ("CHAPS Co"), a private company limited by shares which is owned by its participant Members. CHAPS Co is also the operator of the CHAPS system (that part of the real-time gross settlement system for intra-day sterling payments owned and operated by the Bank of England). To this end, CHAPS Co is responsible for the payment instruction flows across the relevant Participant settlement accounts held at the Bank of England.

The essential characteristics of CHAPS payments are that they are guaranteed (i.e. that once settled over the RT settlement accounts at the Bank of England they cannot be revoked) and they provide same day value.

There are a number of delivery channels available to settlement bank customers (both retail and corporate) initiating CHAPS payments. These payment instructions may be provided by letter, facsimile, telephone, through a Member's own proprietary electronic banking system or, in the case of many financial institutions, via SWIFT, the financial services industry secure network and standards provider. As appropriate to the delivery channel, CHAPS payments may be keyed in at branches, service centres or possibly processed straight through when originated by means of secure electronic systems. Wholesale payments primarily drive CHAPS' daily values and may result from foreign exchange, money market transactions and business-to-business commerce transactions. Business-to-retail and retail-to-retail transactions represent the majority of CHAPS' volumes.

Following prudent authentication and credit checks, the sending bank then transmits the payment through the clearing. Payment details are copied to the Bank of England for settlement in parallel to being transmitted to the receiving settlement bank.

General organisation of the FMI

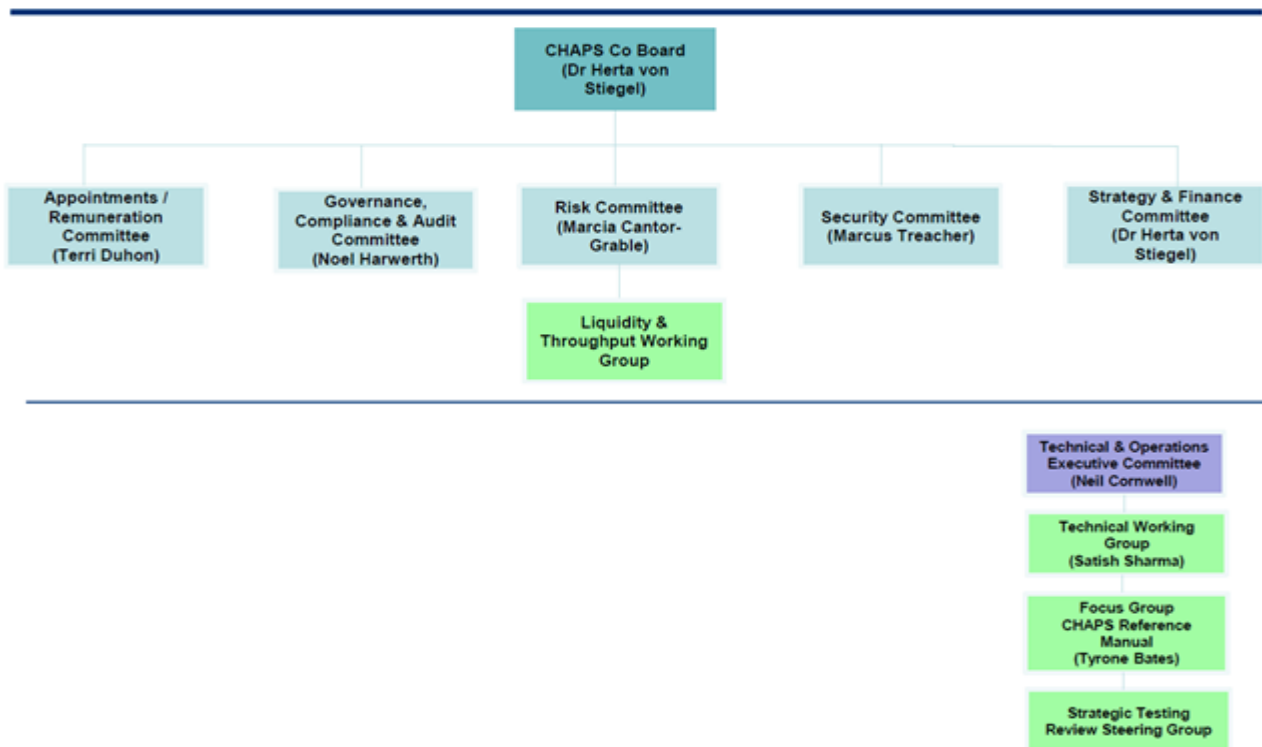
The Company is legally autonomous and has its constitutional arrangements set out in written documentation over which it has exclusive control. The Board of Directors provides oversight for the business of the Company and the Chief Executive Officer, who is responsible for implementing Board policies, attends Board meetings. The Board appoints the Chairman of the Board for a term of three years. The ethos of the Board and the Standing Committees

under it is to work by consensus.

All Board Standing Committees are chaired by Independent Non-Executive Directors and have their own Terms of Reference (ToR) approved and agreed by the Board. The Board and all Committees, and Working groups have a Secretary, one of whose functions is to maintain appropriate records.

The main Committees and their reporting lines as at 28th April 2017 are detailed in the chart below. There are also a number of other sub-committees and working groups shown, which are convened in relation to specific issues or projects.

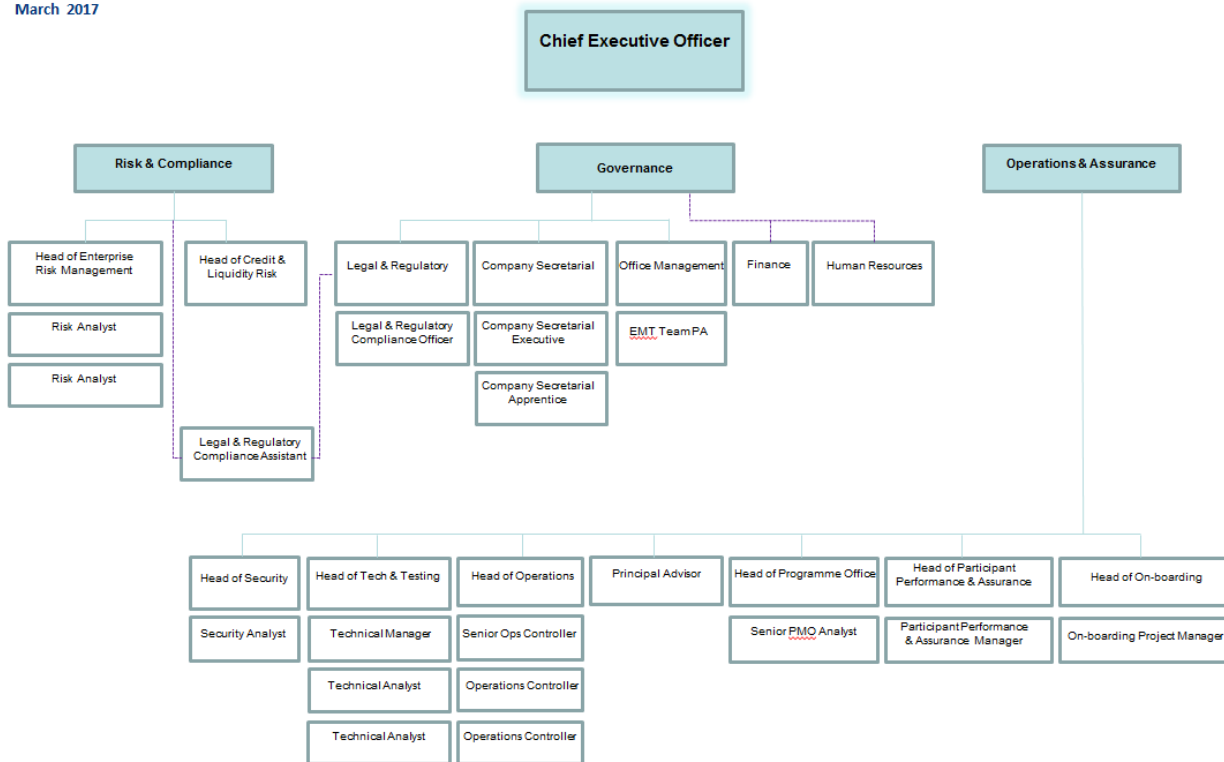
Governance arrangements



CHAPS Co

The business of CHAPS Clearing Company Limited (“the Company”) is managed by the Chief Executive Officer who is accountable to the Board. The Chief Executive Officer is directly supported by a team of 4 people (Chief Operations Officer, Chief Risk Officer and Chief Legal & Regulatory Affairs Officer, Company Secretary) who also form the Company’s Executive Management Team along with the Chief Executive Officer.

The chart below details the Company structure and key areas of responsibility as at 31st March 2017.



CHAPS Co

The Executive Management team³ (EMT) meets weekly to review and approve key management reports and information and to discuss strategy. Additionally there is a Company staff meeting every 4-6 weeks offering the opportunity to brief and debrief all CHAPS Co staff on key matters affecting the work of the Company.

Legal and regulatory framework

Participant Member obligations and responsibilities are clearly articulated in the Company's Memorandum and Articles of Association ("Articles"), the relevant CHAPS Participation Agreement and the CHAPS Reference Manual (containing 'Rules' and 'Procedures'), and the Bank of England Memorandum of Understanding. There is also a legal agreement in place between CHAPS Co and SWIFT governing the provisions of the SWIFT FIN Copy service in relation to CHAPS' management of payment instructions and their related messages.

The requirements for membership of the CHAPS Scheme are set out in the Articles and the Rules (now subsumed into the CHAPS Reference Manual). Additionally, the Company has processes in place to check that defined criteria are met. In essence, Participants are required to be authorised credit institutions (banks or building societies) providing payment services who are able to meet the technical and operational requirements of the clearing. The full membership criteria are published on the Company's website at:

www.chapsco.co.uk

In addition, potential participants must hold a Settlement Account at the Bank of England. Eligibility criteria for Settlement Accounts are maintained by the Bank of England.

³ See details of Company's executive management team at: http://www.chapsco.co.uk/governance/management_team/

CHAPS Co is formally overseen by the Bank of England under the Banking Act 2009. The Scheme is designated as a "system" by the Bank of England, as the relevant designating authority under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (the "SFRs"), which implement the EU Settlement Finality Directive 98/26/EC in the United Kingdom. The designation order was approved by the Bank in May 2000.

The Scheme is also recognised as an inter-bank payment system by HM Treasury under Part 5 of the Banking Act 2009 pursuant to a Recognition Order dated 5th January 2010.

From 1st April 2015 CHAPS Co has also been supervised by the Payment Systems Regulator pursuant to the Financial Services (Banking Reform) Act 2013.

System design and operations

The CHAPS Scheme involves the following major components:

- Participants' payment processes and interfaces to the SWIFT network;
- the SWIFT network and FIN Copy service;
- the Bank of England's RTGS Processor and CHAPS Central Bank Interface to the SWIFT and network; and
- Participants' RTGS Enquiry Link terminals (note however that this component is under a separate agreement with the Bank of England).

Both internal and external customers provide the initial link in the payment process, initiating their payment instructions through a number of channels including, inter alia:

- electronic PC banking products;
- through the branch network;
- facsimile message; and
- SWIFT FIN Network.

Scheme participants are responsible for managing their payment flows and maintaining their settlement account balances at the Bank of England. Responsibility extends through to processing outgoing and incoming payment messages in accordance with current Rules and Procedures contained in the CHAPS Reference Manual.

The SWIFT FIN/FIN copy network connects the participants to the clearing system. The FIN Copy service provides the transport network for the system and the message handling functionality required to convey settlement data to (and receive settlement confirmations from) the Bank of England. SWIFT interfaces, known as CBTs (Computer Based Terminals), are located within participants' systems to connect to the network and process messages to and from their payment systems.

The Bank of England (through its Real Time Gross Settlement system) controls the settlement accounting processes within its own systems and is responsible for the RTGS processor.

IV. Principle-by-principle summary narrative disclosure

The following represents an updated summary narrative of the full disclosure presented to the Bank of England earlier this year and represents the Company's position as at 20th August 2017. Out of the 16 principles that CHAPS Co has assessed itself against, the Company has marked itself as fully compliant with 13 principles and partially compliant with 3 principles [Chart 1].

In order to assist the reader with the methodology employed with respect to the overall risk rating, a principle has flagged green (i.e. fully compliant) *only if* each consideration and question within that principle has also been marked green. This means, for example, that there may be principles marked amber which are highly likely to turn to green upon completion of one or two minor actions.

Looking more closely, out of a total population of 207 questions, the Company has marked itself as fully compliant against 204 questions (96%) and partially compliant against 3 questions (4%). There are no instances of non-compliance listed against the Company's self-assessment [Chart 2].

Chart 1

IOSCO Principles	24
CHAPS Co Applicable	16
Fully Compliant	13
Partially Compliant	3

Chart 2

Total Questions	207
Fully Compliant	204
Partially Compliant	3
Not Compliant	0

Principle 1 – Legal Basis

An FMI should have a well founded, clear, transparent, and enforceable legal basis for each material aspect of its activities in all relevant jurisdictions.

Summary

CHAPS Co has a well-founded, clear, transparent and enforceable legal basis for each material aspect of its activities in all relevant jurisdictions. In particular, designation of the CHAPS scheme under the SF Directive ensures that the Scheme is afforded the key protection of this legislation, namely finality of settlement of payments entered into the CHAPS system.

Additionally, a robust process is in place with respect to obtaining legal opinions for all Participant jurisdictions, with the same being reviewed by both CHAPS Co Chief Legal & Regulatory Affairs Officer and the Bank of England legal functions. Where necessary, external specialist counsel is also engaged.

After an extensive consultation and implementation process, CHAPS Co and all Direct Participants adopted the CHAPS Reference Manual on 13th February 2017. The CHAPS Reference Manual clearly codifies and consolidates all key obligations into one document. This in turn continues to ensure consistency and clarity by clearly outlining the legal relationship and responsibilities between participants and the Scheme as well as, where applicable, the legal relationship as between participants *inter se*. Chapter 2 of the CHAPS Reference Manual continues to be aligned with the Bank of England's RTGS Terms of Reference (in particular, with the definitions therein relating to settlement finality) in order to ensure consistency and clarity.

RAG Status

Fully Compliant

Green: 10/10

Amber: 0/10

Red: 0/10

Principle 2 – Governance

An FMI 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.

Summary

CHAPS Co's Memorandum and Articles of Association⁴ continues to support and incorporate provisions relating to increased independent presence on the CHAPS Co Board⁵ and matters of public interest being considered. In a similar vein, the Governance, Compliance and Audit Committee, Strategy and Finance Committee, Strategy Committee, Appointments and Remuneration Committee and the Risk Committee are each chaired by Independent Non-Executive Directors (INEDs). With the Independent Chair, INED and Company Secretarial roles now firmly established, the Company continues to maintain observation of this principle. A review of the Committee structure was undertaken in the second half of 2016 and changes were made to enhance governance effectiveness.

RAG Status

Fully Compliant

Green: 26/26

Amber: 0/26

Red: 0/26

⁴ See CHAPS Co Memorandum and Articles of Association at: <http://www.chapsco.co.uk/governance/key-documentation>
⁵ Currently chaired by an Independent Chairman and supported by four Independent Directors.

Principle 3 - Framework for the comprehensive management of risks

An FMI should have a sound risk-management framework for comprehensively managing legal, credit, liquidity, operational and other risks.

Summary**RAG Status**

CHAPS Co has a comprehensive risk framework setting out its approach to risk identification, measurement, management and reporting. Risks are identified in the Risk Framework taking a top down approach with risk tolerance and appetite recommended by the Risk Committee and reviewed and endorsed by CHAPS Co Board on an annual basis (last review July 2016).

Fully Compliant

Green: 19/19
Amber: 0/19
Red: 0/19

Principle 4 – Credit Risk

An FMI should effectively measure, monitor, and manage its credit exposure to participants and those arising from its payment, clearing, and settlement processes. An FMI should maintain sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence.

Summary**RAG Status**

CHAPS Co is compliant with this principle.

Fully Compliant

Green: 11/11
Amber: 0/11
Red: 0/11

Principle 7 – Liquidity Risk

An FMI should effectively measure, monitor, and manage its liquidity risk. An FMI should maintain sufficient liquid resources in all relevant currencies to effect same-day and, where appropriate, intraday and multiday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the participant and its affiliates that would generate the largest aggregate liquidity obligation for the FMI in extreme but plausible market conditions.

Summary**RAG Status**

As a PvP system, many of these considerations are not directly applicable to CHAPS Co itself; however, where relevant, we have indicated where we believe the considerations impact CHAPS Co Participants. The implementation of a payment database allows more detailed reporting and analysis of payment flows, however whilst the tools have been developed they are yet to be deployed in production outside of ad-hoc trigger event monitoring.

Partially Compliant

Green: 9/10
Amber: 1/10
Red: 0/10

Principle 8 - Settlement Finality

An FMI should provide clear and certain final settlement, at a minimum by the end of the value date. Where necessary or preferable, an FMI should provide final settlement intraday or in real time.

Summary

RAG Status

Payment is irrevocable at the point of entry of the payment message into the CHAPS system. This is also clearly identified within the CHAPS Co Rules and is underpinned by the provisions of the SF Directive (see also summary at Principle 1 which also notes alignment with the Bank of England's RTGS provisions with respect to settlement finality).

Green: 13/13
Amber: 0/13
Red: 0/13

Principle 9 - Money Settlements

An FMI should conduct its money settlements in central bank money where practical and available. If central bank money is not used, an FMI should minimise and strictly control the credit and liquidity risk arising from the use of commercial bank money.

Summary

RAG Status

Although relevant to payment systems generally, this principle is not relevant to CHAPS Co as CHAPS only settles in central bank money in pounds sterling.

Fully Compliant

Green: 2/2
Amber: 0/2
Red: 0/2

Principle 13 - Participant-Default Rules and Procedures

An FMI should have effective and clearly defined rules and procedures to manage a participant default. These rules and procedures should be designed to ensure that the FMI can take timely action to contain losses and liquidity pressures and continue to meet its obligations.

Summary

RAG Status

The Company observes this principle as underpinned by its robust CHAPS Reference Manual⁶ which all scheme participants sign up to upon joining the Scheme. Additionally, and in consultation with the Bank of England, the CHAPS Reference Manual has been amended to support, where appropriate and with relevant legal and risk considerations, continuity of access to payment systems in the event of a Participant default as defined or anticipated by the Rules.

Fully Compliant

Green: 11/11
Amber: 0/11
Red: 0/11

⁶ See CHAPS Reference Manual at: <http://www.chapsco.co.uk/governance/key-documentation>

Principle 15 – General Business Risk

An FMI should identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialise. Further, liquid net assets should at all times be sufficient to ensure a recovery or orderly wind-down of critical operations and services.

Summary

RAG Status

CHAPS Co has procedures in place to monitor its general business risk and to capture emerging risks as part of the Company's overall risk framework. CHAPS Co has established and maintains segregated reserves for use in a recovery⁶ or resolution situation. Additionally, CHAPS Co has a Recovery Plan that identifies potential scenarios that may endanger Scheme viability, identifies early warning indicators that allow timely recognition of such events crystallising and sets out potential recovery⁷ options. It places appropriate Board led governance around recovery plan activation and monitoring. The Company also has an appropriate CHAPS Co Resolution Framework Document in place which is aligned with the resolution tools given to HM Treasury under SAR.

Fully Compliant

Green : 13/13

Amber: 0/13

Red: 0/13

Principle 16 – Custody and Investment Risks

An FMI should safeguard its own and its participants' assets and minimise the risk of loss on and delay in access to these assets. An FMI's investments should be in instruments with minimal credit, market, and liquidity risks.

Summary

RAG Status

CHAPS Co holds no monies on behalf of its Participants in a custody context. In terms of custodians used for its reserves, CHAPS Co relies upon well-established UK and Globally Significant banks holding highly liquid (i.e. cash), easily accessible assets.

Fully Compliant

Green: 10/10

Amber: 0/10

Red: 0/10

⁷ Regulatory reserves established within the Company's Rules. These exceed six months' of operating costs and are reviewed on an annual basis. In addition, minimum operational reserves are also held to a level set by the CHAPS Board which is also reviewed on an annual basis.

Principle 17 - Operational risk

An FMI should identify the plausible sources of operational risk, both internal and external, and mitigate their impact through the use of appropriate systems, policies, procedures, and controls. Systems should be designed to ensure a high degree of security and operational reliability and should have adequate, scalable capacity. Business continuity management should aim for timely recovery of operations and fulfilment of the FMI's obligations, including in the event of a wide- scale or major disruption.

Summary

RAG Status

CHAPS Co has a comprehensive operational risk assessment process in place which identifies emerging risks, regularly assess existing risks and controls and which subjects the Company and Scheme to a range of extreme but plausible risk scenarios and stress events. This is supplemented by a regular testing programme of contingency and business continuity solutions involving CHAPS Co, Scheme participants and key suppliers.

The RTGS that the CHAPS Settlement System operates on, is owned and operated by the Bank of England. The messaging systems that connect Participants to the CHAPS Settlement System are owned and operated by SWIFT with individual participant systems provided by the member organisations.

Both the settlement system and the messaging systems are provided on an arm's length basis to CHAPS Co; under contract in the case of SWIFT as part of their core service schedule and under a Memorandum Of Understanding in the case of the Bank of England. In both cases, each organisation has responsibility for the design, security, maintenance and operations of the systems for which it is responsible.

Comfort regarding risk management is therefore obtained through the following assurance processes:

- The ISAE3402 process undertaken by both SWIFT and the Bank of England;
- The oversight process undertaken in respect of SWIFT by the National Bank of Belgium, which involves the Bank of England; and
- Other accreditations and disclosures, such as CPMI Principles for FMIs and Critical Service Providers.

Additional risk assessment and assurance is carried out via regular relationship management between CHAPS Co and the Bank of England and CHAPS Co and SWIFT to the extent that it is permissible and appropriate. Following a strategic review of the engagement between RTGS/CHAPS Co. a number of recommendations were made which both parties actively delivered. In September 2016 CHAPS established a Joint Risk Forum between Bank of England RTGS team and CHAPS to discuss common risk issues and monitor mitigation activities. Risk liaison between CHAPS and SWIFT has also deepened since the previous period, with significant liaison on the implementation of SWIFT's Customer Security Programme and the implications for CHAPS Direct Participants.

One of the key benefits of a single operator model (as announced by the Bank of England in May 2017) is to allow access to more risk information, enabling more effective end-to-end systemic risk management in relation to key service infrastructure.

Participant Banks remain subject to the Rules, Requirements and Procedures documented within the CHAPS Reference Manual. A significant update was delivered in February 2017. Part of this defines the requirements for participants with respect to resilience, fail over and business continuity. Resiliency expectations were further

Partially Compliant

Green: 30 /31

Amber: 1 /31

Red: 0/31

enhanced in this version of the manual.	
Principle 18 - Access and participation requirements An FMI should have objective, risk-based, and publicly disclosed criteria for participation, which permit fair and open access.	
Summary	RAG Status
<p>The Company fully observes this principle by publicly disclosing its objective, risk based criteria and rules⁸ which permit fair and open access and participation in the scheme. Additionally, the Company is required to attest to similar pursuant to the Payments Systems Regulator’s Access and Reporting Rules on an annual basis.</p> <p>The Company’s revised Rule set (now consolidated in the CHAPS Reference Manual), also includes a more granular breakdown of requirements identified via Participant categorisation i.e. broadly, requirements will be aligned according to a Participant’s relative risk to both the CHAPS payment system and wider financial ecosystem.</p>	Fully Compliant Green: 11/11 Amber: 0/11 Red: 0/11
Principle 19 – Tiered participation arrangements An FMI should identify, monitor, and manage the material risks to the FMI arising from tiered participation arrangements.	
Summary	RAG Status
<p>CHAPS Co has continued to make significant progress with respect to reducing the tiered nature of the scheme with a number of material indirect participants committing to direct participation during the 2016-2017 period. There remains one indirect participant in breach of the Tiering Criteria, however they are scheduled to on-board in 2018.</p> <p>The Company’s rules continue to be clear and transparent with respect to tiering thresholds and the Company’s obligations with respect to ensuring that de-tiering remains of critical importance to the systemic stability of the payments landscape.</p>	Fully Compliant Green: 9/9 Amber: 0/9 Red: 0/9

⁸ See CHAPS joining requirements at: <http://www.chapsco.co.uk/access/access-chaps>

Principle 21 - Efficiency and effectiveness

An FMI should be efficient and effective in meeting the requirements of its participants and the markets it serves.

Summary

CHAPS Co has implemented numerous methods to track both efficiency and effectiveness through extensive company-wide Key Performance Metrics that are governed through Executive Management Team process, and reviewed periodically by Relevant Committees and Board.

Through taking data points from across the industry, peer group and wider CHAPS continues to challenge itself to perform at industry best in class driving continual improvements through its transformational signature actions that underpin the delivery of the CHAPS strategy.

Critical examples of this are measured productivity improvements over the last 18 months of c 30% along with increases in the volume of onboarders (from 1 or 2 per year to up to potentially 8 per year) without proportionate effort/cost increases. Industry leading practices for Participant Assurance are being implemented focusing on both the efficiency of the execution for the Direct Participant whilst enhancing the focus and level on information thereby driving up effectiveness.

Additionally, the Company is committed to ensuring that its service meets the various needs of all of its stakeholders and it therefore maintains an active and open dialogue with those that are directly involved in providing the current service. To ensure that this remains the case the Company directly engages with all of its service users via the Service User Group. Participation in this Group is open and enquiries for application are invited directly from the Company's website.

All recommendations detailed in the Deloitte report covering the 20th October 2014 outage were addressed and implemented where necessary by the end of 2016.

Efficiency and effectiveness will continue to underpin our revised strategy as we progress through to 2020.

RAG Status**Partially Compliant**

Green: 6/7

Amber: 1/7

Red: 0/7

Principle 22 - Communication procedures and standards

An FMI should use, or at a minimum accommodate, relevant internationally accepted communication procedures and standards in order to facilitate efficient payment, clearing, settlement, and recording.

Summary

Use of the SWIFT network with Closed User Group functionality ensures that CHAPS Co is fully compliant with this principle.

RAG Status**Fully Compliant**

Green: 5/5

Amber: 0/5

Red: 0/5

Principle 23 - Disclosure of rules, key procedures, and market data

An FMI should have clear and comprehensive rules and procedures and should provide sufficient information to enable participants to have an accurate understanding of the risks, fees, and other material costs they incur by participating in the FMI. All relevant rules and key procedures should be publicly disclosed.

Summary

RAG Status

The CHAPS Reference Manual published on the Company's website in February 2017 consolidates the strong rule set, key operational requirements, procedures and processes that apply to the Scheme's Direct Participants and is publically accessible to all website visitors and Participants. The Company therefore considers itself fully compliant with this principle.

Fully Compliant

Green: 19/19

Amber: 0/19

Red: 0/19

V. List of publicly available resources

The following list of publicly available resources may also assist the reader with understanding more about CHAPS Co and its approach to observing each applicable principle noted in the summary narrative disclosure above.

CHAPS Co website: www.chapsco.co.uk

CHAPS Core Key Governance Documents (Rules, Tiering Criteria, Throughput Criteria, Memorandum and Articles of Association, Board Terms of Reference and Minutes, Committee Structure, CHAPS Co Market Report and Financial Statement):

http://www.chapsco.co.uk/governance/governance_documents/

CHAPS joining requirements: <http://www.chapsco.co.uk/access/access-chaps>

Payments UK website: <http://www.paymentsuk.org.uk/>

The Bank of England website: <http://www.bankofengland.co.uk/Pages/home.aspx>

The Bank of England's supervision of financial market infrastructures -Annual Report March 2016-February 2017⁸:

<http://www.bankofengland.co.uk/publications/Documents/fmi/annualreport2017.pdf>

Standards for financial market

infrastructure: <http://www.bankofengland.co.uk/financialstability/Pages/fmis/standards/requirements.aspx>

HM Treasury: <http://www.hm-treasury.gov.uk/>

HMT Consultation on Implementation of the revised EU Payment Services Directive (PSDII): https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/589023/implementation_of_revised_EU_directive.pdf

HMT Consultation on draft innovation plan for financial services: <https://www.gov.uk/government/consultations/consultation-on-draft-innovation-plan-for-financial-services/consultation-paper-on-draft-innovation-for-financial-services>

CHAPS Co response to “*Opening up UK Payments*”:
http://www.chapsco.co.uk/governance/legal_and_regulatory_landscape/regulatory_responses/

CHAPS Co response to “*Special administration regime for payment and settlement systems*”:
http://www.chapsco.co.uk/governance/legal_and_regulatory_landscape/regulatory_responses/

CPSS-IOSCO “*Principles for financial market infrastructures*” (April 2012):
<http://www.bis.org/publ/cpss101a.pdf>

CPSS-IOSCO Disclosure framework for financial market infrastructures – Consultative Report

(April 2012): <http://www.bis.org/publ/cpss101c.pdf>

CPSS-IOSCO Disclosure Framework and Assessment Methodology (December 2012):
<http://www.bis.org/publ/cpss106.pdf>

The Bank of England Quarterly Bulletin 2013 Q4 “*Tiering in CHAPS*”:
<http://www.bankofengland.co.uk/publications/Documents/quarterlybulletin/2013/qb130408.pdf>

The Financial Markets Law Committee website:
<http://www.fmlc.org/Pages/home.aspx>

The Payment Systems Regulator’s regulatory framework and approach (published 25.03.15):
<https://www.psr.org.uk/psr-publications/policy-statements/policy-statement-151>

The Payment Systems Regulator’s webpage on governance of payment systems:
<https://www.psr.org.uk/psr-focus/governance-payment-systems>

PSR Access and governance report on payment systems
2017: <https://www.psr.org.uk/sites/default/files/media/PDF/Access-and-governance-report-March-2017.pdf>.

Payment Systems Regulator Annual Plan and Budget for
2017/18: <https://www.psr.org.uk/sites/default/files/media/PDF/Annual-plan-and-budget-2017-2018.pdf>

2016/2017 CHAPS Co response to the Payments Systems Regulator’s consultations;

Guidance on CHAPS Co’s approach to handling applications under sections 56 and 57 of the
Financial Services (Banking Reform) Act 2013:
http://www.chapsco.co.uk/sites/default/files/chaps_co_response_psr_jul_16.pdf

Response to the Payments Strategy Forum – Being Responsive to User Needs:
http://www.chapsco.co.uk/sites/default/files/chaps_co_response_to_the_psf_consultation.pdf

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