

## **BBA Response to Consultation on ESMA Guidelines on participant default rules and procedures**

**30 June 2016**

### **Executive Summary**

The British Bankers' Association (BBA) welcomes the opportunity to engage with ESMA on their guidelines on participant default rules and procedures under CSDR. The BBA supports the approach taken by ESMA in consulting with relevant stakeholders on these guidelines, and looks forward to engaging with ESMA on this matter further in future.

The BBA is the leading association for the United Kingdom banking and financial services sector, representing over 200 banks which are headquartered in 50 countries and have operations in 180 countries worldwide. Our members manage more than €10 trillion in banking assets, employ nearly half a million individuals, contribute some €100 billion to the economy each year and lend some €200 billion to businesses.

The BBA broadly supports the proposals put forward by ESMA. We consider that the actions listed in the guidelines and the testing and reviewing procedures are appropriate, although in the case of the latter we recommend that discussions around insolvency proceedings be extended to include "indirect participants".

We have suggested multiple stakeholders who should be involved in the definition of the default rules and procedures of a CSD, and a number of items that should be included in the internal plans. We believe these suggestions would help to safeguard the position of CSDs and would put CSDs in a strong position to defend themselves against defaults.

In addition, we recommend that any participant, or its designated authority, should be obligated to notify their CSD about defaults in a timely manner so as to minimise risk for both CSD and participant. We do not believe any additional steps need to be taken over transmitting information on implementation of default rules to stakeholders, as through insolvency proceedings this will automatically be a matter of public record and will therefore not require any additional publicising.

## Questions

**1. Do you consider other stakeholders should be involved in the definition of the default rules and procedures of a CSD? If so, which ones, and what should be the level of their involvement?**

Other stakeholders should be involved in the definition of the default rules and procedures of a CSD. Their level of involvement should be in an advisory capacity, as the final decision will be for the CSD to determine, subject to the requirements of national law.

The BBA would recommend that consideration be given to including the following stakeholders in deciding the definition of the default rules and procedures of a CSD:

- National securities regulators;
- Brokers connected to the CSD;
- Custodians connected to the CSD;
- National central bank;
- National insolvency service;
- Secured creditors of the CSD.

**2. Do you think that such acknowledgement process is appropriate? In particular, do you consider it necessary for the CSD to verify the information regarding the default with the designated authority under the SFD before the CSD can take any action, or should the CSD be able to start taking actions based on its reasonable assessment of the participant's situation and on the reliability of the source that informed the CSD in the first place?**

The BBA believes that such acknowledgement processes are appropriate, although we recommend that a defaulting participant should be required at the same time as advising the CSD to advise the national competent authority. This would ensure there was no delay by the CSD in relaying any information to the national competent authority.

The default should be advised by a confirmed method of communication, for example a court document or a secure electronic message. This will avoid the delay involved by subsequent verification. ESMA could best assess these methods by referring to existing practice in Member States, where defaults of commercial organisations have been routinely, but confidently, advised on a daily basis for many decades.

We support ESMA's proposal that the participant itself or its designated authority under the Settlement Finality Directive (SFD) should notify the CSD about the default. This notification should take place in a timely manner so as to minimise the chances of risk for the CSD and its participants.

**3. Do you consider that the actions listed are appropriate or that other actions should be listed? Should certain actions be mandatory, depending for instance on the type or size of default, the characteristics of the participant of the CSD or any other criteria?**

The BBA considers that the actions listed are appropriate.

#### **4. Do you think other items should be included in the internal plans?**

There are multiple items that should be included within the internal plans, in order to safeguard the CSD's position against the defaulting participant. These include, but are not limited to the following:

- Claims and potential counter-claims;
- Enforceability of secured claims and charges;
- Liens;
- Reservation of title;
- Access to data;
- Key employees;
- Physical security of assets;
- Signatories over assets;
- Net positions, close-out netting, and potential danger of net positions being grossed up;
- Impact upon the CSD's ability to continue its own operations.

The BBA believes that the inclusion of these items in the internal plans would put CSDs in a strong position to safeguard themselves against a participant who has defaulted or in the process of defaulting. In addition, we recommend that ESMA place these plans under period review, as legal frameworks are likely to change over time.

We also believe that ESMA should clarify the position of non-defaulting participants not directly affected by the default. Such participants should not be within the scope of Paragraph 23. Non-defaulting participants are not liable for other defaulting participants, and they therefore have no role to play in default procedures unless they are affected by the defaulting participant's default, for example via pending transactions.

#### **5. Do you think that information on the implementation of the default rules and procedures should be transmitted to other stakeholders? If so, which other stakeholders?**

Information on the implementation of the default rules and procedures shall be a matter of public notice, since the participant will have entered insolvency proceedings (which are a matter of public record), and these proceedings will automatically trigger the CSD's default procedures.

The BBA therefore cannot see any reason why this information on implementation should be transmitted to other stakeholders, as it will be made a matter of public record by virtue of the process described above.

#### **6. Do you think that such testing and reviewing processes are appropriate?**

The BBA believes that these testing and reviewing processes appear appropriate. We believe that it should also involve the custodians and/or settlement agents for where there are concerns of a possible default scenario involving a client of a CSD participant. These testing activities should also involve the relevant authorities managing the default.

Provided CSDs are kept informed of the identities of indirect participants, which is already the case in some markets where these participants are active as trading members, then we see no reason why discussions around insolvency procedures should not be extended to also include "indirect" participants as outlined in Article 2 of the SFD:

“Indirect participant shall mean an institution, a central counterparty, a settlement agent, a clearing house or a systems operator with a contractual relationship with a participant in a system executing transfer orders which enables the indirect participant to pass transfer orders through the system, provided that the indirect participant is known to the system operator”.