

Paris, October 31, 2003

## **CONSULTATIVE REPORT**

### **Standards for securities clearing and settlement systems In the European Union**

The FBF, or French Banking Federation, the French professional body which represents all banks operating in France (over 500 commercial, cooperative or mutual banks), welcomes the ESCB-CESR public consultation relating to its proposed standards for securities clearing and settlement systems in the European Union.

The FBF fully agrees with the objective of the ESCB-CESR standards for securities clearing and settlement which is to minimise risks for all European participants and thus ensure the stability of the European Union's financial markets. The FBF also welcomes the fact that the standards that will apply to the European Union are very similar in content to the CPSS/IOSCO recommendations.

However, the FBF notes that, contrary to the CPSS/IOSCO recommendations, the scope of parties concerned by this proposal has been extended, for no valid reason, beyond the securities market infrastructure (CCP, CSD) and that, on the other hand, the proposals are no longer recommendations, but rather standards.

On a more fundamental level, the approach adopted, consisting in the definition of functions without regard to post-trading institutional structures, leads the authors of the report to eliminate certain obvious boundaries which exist between securities market intermediaries and infrastructures.

This confusion will lead CSDs to extend their infrastructure activities, which do not by nature pose any risk, to those of financial intermediaries, thereby generating a structural increase in overall potential risks that is entirely opposed to the report's objective of mitigating risk.

The FBF understands that the European regulatory authorities have to take into account the historical specificity of the European post-trade model, where CSDs established and regulated in each country in the Union exist alongside two ICSD from the unregulated eurobond market. However, the French banks feel it would be dangerous in terms of both risk and competition, to allow this specificity to become the reference. Indeed, the ESCB-CESR proposal aims to integrate infrastructure and intermediary activities which, with the exception of ICSDs, are currently separated, whereas the secure risk model consists in restricting the activities of CSDs, to prevent them from taking financial risks.

In terms of competition, it should also be noted that the infrastructures in the European market for post-trade operators are currently consolidating and occupy dominant positions in their market segment, by virtue of their status as essential facilities, whereas the custodian establishments operate in a highly competitive environment.

In our view, the ESCB-CESR group's proposal completely contradicts recent evolutions in Europe in the field of general economic networks and services. In fact, the European legislator has gradually separated infrastructure activities from competitive activities in order to open the domestic market up to competition while preventing abuses on the part of the infrastructure.

Furthermore, the provisions proposed by the ESCB-CESR group also raise questions as to their impact, not only on the European market, but also on trans-Atlantic dialogue:

- the divergence of the European model from the standard international model defined in the G30 report of 1989,
- the concentration of risk in European infrastructure, when the G30 group itself addresses the issue of the interconnection and global security of financial markets in its report of January 2003,
- the evaporation of the liquidity provided by custodian banks to US traders, the obligation for international custodians to separate their European positions from international positions held on behalf of their clients.

For all the above reasons, the FBF recommends that the underlying model to be adopted for the application of European standards clearly separate infrastructure and intermediary functions.

Since this distinction falls within the competence of the European Commission, as relating to the Domestic Market and Competition Policy, the ESCB-CESR Group proposal is in our view premature: it should follow on from, and not precede, the legislative provisions of the Commission. In addition, the proposal appears to fall outside the scope of the institutional group's mandate.

A different functional approach could be adopted to apply standards to the ICSDs, CSDs and custodian banks, without at the same time encouraging infrastructures to develop activities such as credit or securities lending, which are not compatible with their initial vocation due to the systemic risk they entail.

As a result of this observation, the FBF wishes to propose another method of distinguishing between the various post-trade participants:

the fundamental difference between a CSD and a custodian resides in the fact that a CSD must act as an infrastructure for the entire market, on the basis of a system of "membership" (indeed, market infrastructures are seen as a means of generating economies of scale without market risks), whereas custodians serve the interests of their clients who thus gain access to the infrastructure. In this context, we feel it is unrealistic to try to regulate these two functions using the same model. They are not on the same level, do not offer the same services (collective services to members on the one hand, and individual services to clients on the other) and are not intended for the same users (financial intermediaries in the case of CSDs, all market participants for custodians i.e. issuers, investors, intermediaries).

The FBF therefore proposes that the standards be applied differently according to the function carried out by the participant in question<sup>1</sup> (annexe I), which include:

1. guarantee functions (CCPs)
2. functions associated with a notary role (CSD for all activities and ICSDs for part of their activities only)
3. added value activities (custodians and ICSDs for the remainder of their activities).

ICSDs are mixed institutions, which means that they carry out both notary and banking activities, and are obliged to comply with the standards applicable to both their fields of activity.

With respect to the functions associated with banking activities, the report makes reference to "custodians which may trigger systemic risk" due to the volumes they process, but provides no real explanation of the concept.

The FBF points out that this banking activity is already subject to prudential ratios which specifically target all types of risk: credit risk, market risk, liquidity risk. Furthermore, the Basel Committee and the future European capital adequacy ratio have defined specific requirements to cover operational risk arising from this particular activity, by including custodian activities (Appendices H-3, H-4) (annex II) in the scope of the activities of Agents in its standardised approach. Moreover, it would no doubt be preferable that this category of custodians adopt the so-called Advanced Measurement Approach, according to size criteria. European custodians are also subject to regulations imposed by CSDs and CCPs on their participants (operational and financial criteria), and even, by extension, to the restrictions by

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<sup>1</sup> The appendix I contains an extract of the FBF's comments on the Commission's communication relating to securities clearing and settlement mechanisms in the European Union, which specified the different functions of the post-trade participants and proposed European regulations that they should observe.

which their clients are bound under US legislation on pension funds (protection of assets and service continuity).

Furthermore, it must also be stressed that there is a specific procedure for managing the systemic risk potentially posed by a custodian by virtue of its size, as the European capital adequacy project of July 2003 specifies in Article 126(2) (annexe III), appended hereto, that the competent authorities have a procedure for evaluating this risk and may, under Pillar II, impose specific capital adequacy requirements.

In the US, "the board of Governors of the Federal Reserve System and Securities and Exchange Commission's interagency" used this concept in its white paper on the structural modification of settlement systems for government borrowing, but only in order to define specific rules to be applied to ensure the security of the operational procedures, as it rightly considered that the financial risk was adequately managed using the prudential ratios and that, contrary to the proposals of the report, corporate governance, transparency and access to custodians are in fact dictated by the competitive market.

In its recommendation 13 (report of January 2003), the Group of 30 adopts the same logic with its section "Address the possibility of Failure of a systemically important institution", which focuses on the risk of interruption of an operator's service. The Group of 30 does not recommend the use of this concept for any risks other than operational risks such as financial failure. The G 30 report clearly recognises that many recommendations can be applied to the operation of institutions carrying out settlement activities but that prudential regulations currently in force or scheduled to be adopted are sufficient for banks.

The FBF therefore considers that in the case of custodians, regardless of whether they pose a systemic risk, a complete system already exists or is pending for the supervisory authorities which will meet the concerns expressed in the report. This system has already been the object of extensive study both at European and international level and has been approved by the credit establishments subsequent to various statistical tests which took into account the different types of risk.

It is therefore completely inappropriate not only to include custodians in the scope of application of the standards, but above all to place them on the same level as CSDs and ICSDs.

In general, the FBF deems that the proposed standards should apply to CCDs, CCPs, and ICSDs due to their infrastructure role, but not to custodian banks. We are not opposed to the establishment of specific standards for the banking profession, relating to operational and custodian risks (standards 11 and 12, operational reliability and custody risk), provided the ESCB-CESR Group can show that its proposals on these issues do not reiterate the existing legislation (DSI Directive and Banking Regulations).

Moreover, in general, the FBF approves of the standards to be applied to CSDs which correspond to the CPSS-IOSCO recommendations, but considers that the standards (5, 6, 9, 10), which would be exceptions in the international settlement landscape, carry new risks (legal, market and liquidity risks). Similarly, standards 1, 8, 18, 19 (legal framework, settlement finality, regulation and oversight, cross-border links) relate exclusively to CCPs and CSDs.

The FBF also approves of the need for standards (13, 14, 15 and 17) concerning corporate governance, access to, efficiency and transparency of infrastructures but considers them completely inappropriate for custodians operating in a competitive environment.

Furthermore, standards 2, 3, 4, 7, 16 (trade confirmation, CCPs, settlement cycle, delivery versus payment, communication procedure) relate exclusively to CCPs and CSDs, but in our view these measures should be determined by market decisions rather than regulatory standards.

Finally, the FBF understands the observations on dominant positions. Indeed, it is dangerous for a market participant, or more specifically, an infrastructure, to be able to dictate its conditions to other market users by virtue of its position, and create competitive distortions. However, under the framework proposed by the FBF, the CSDs, as we define them, are not supposed to impose conditions if they have a monopolistic position, but rather provide a service which is in the general interest.

Similarly, given the intense competition in the sector, no European custodian could today be deemed to have a dominant position and, in any case, all custodians are subject to competition regulations. We feel these criteria are inappropriate in the context of standards, and should be left to the competition authorities, under the scope of legislation relating specifically to securities clearing and settlement.



In conclusion, the FBF approves of the majority of the proposed standards, insofar as they take into account the prudential rules already implemented, but disapproves of the underlying reference model for post-trading activities, which defines the scope of application for these standards. It is inappropriate and generates additional potential risks, undermining the initial objectives of the standards.

In the FBF's view, it is vital that this work on the standards form part of a European directive on post-trading activities.

***Standard 1 : Legal framework***

***Securities clearing and settlement systems and links between them should have a well - founded, clear and transparent legal basis in the relevant jurisdictions.***

**Addressees: CSDs, CCPs and custodians operating systemically important systems.**

***Response:***

In relation to the legal framework, FBF supports all measures intended to create a secure community framework within the European Union for all post-trade participants. However, this legal framework must clearly take into account each post-trading activity: businesses providing added value services (all custodians including ICSDs for their banking business), notary activities (CSD's and ICSD's notary activities), and guarantee activities (CCPs).

While the FBF clearly accepts that a legal framework is required for all participants, it nonetheless believes it is important to distinguish between the following:

- on the one hand, the custodians – which manage their client relationships on the basis of contractual agreements and are already governed and controlled by banking supervisory authorities – for which FBF feels only a single set of specifications for "securities account holders - custodians" needs to be imposed at European level.
- on the other hand, the market infrastructure, the roles and responsibilities of which need to be accurately defined, and notably their relationships with their members.

With respect to ICSDs, which carry out added value activities (incurring risk on behalf of their clients), and notary activities (without risk exposure), we would suggest that the regulatory framework restrict their activities and establish a specific set of regulations.

In conclusion, while supporting the CESR – ECB's objective to create a common legal framework, the FBF requests that the framework cover all post-trade participants, including all custodians, but at the same time distinguish clearly between them on the basis of their activities.

***Standard 2 : Trade confirmation and settlement matching***

***Trades between direct market participants should be confirmed without delay after trade execution, and no later than trade date (T+0). Where confirmation of trades by indirect market participants (such as institutional investors) is required, it should occur as soon as possible after trade execution, and no later than T+1.***

***For settlement cycles that extend beyond T+0, settlement instructions should be matched as soon as possible and no later than the day before the specified settlement date.***

***Addressees: Market participants and operators of systems for trade confirmation, affirmation and matching of settlement instructions.***

***Response:***

The FBF fully agrees with the need for a standard which requires that trades be confirmed "without delay" and no later than "the trade date", and that settlement instructions be matched as soon as possible and no later than the day before the specified settlement date (except in the case of value today transactions).

**Key element 3:** however, the FBF has reservations over the legal value of a "trade confirmation", notably when the two counterparties are located in different countries, and feels that this matter could be resolved with the use of standard agreement models, drawn up by sector professionals, similar to those used for certain types of transaction (e.g.: securities borrowing/lending in France). The FBF also feels that the objective of obtaining confirmations from indirect participants at T+0 is unrealistic.

**Key element 5:** with regard to "settlement matching", as there are several practices currently used in the European Union, all parties concerned need to move towards harmonisation before this standard can be implemented, although without adopting a unique method. The responsibilities for matching between custodians will have to be clearly defined, as will those for SSS operators and custodians.

As regards the addressees, this standard should indeed be aimed at all market participants and associated operators.



***Standard 3 : Settlement cycles***

***Rolling settlement should be adopted in all securities markets. Final settlement should occur no later than T+3. The benefits and costs of an EU-wide settlement cycle shorter than T+3 should be evaluated.***

***Addressees: CSDs CCPs and custodians that operates systemically important systems and operators of regulated markets.***

***Response:***

The FBF is very much in favour of this standard for regulated markets where, to the best of its knowledge, it is already a widely used practice. However, this standard cannot be applied to OTC transactions.

**Key element 2:** as regards the draft standard for settlement at T+3, FBF has no comments to make, since this deadline is already standard practice in France.

**Key element 3:** on the other hand, in the context of European harmonisation, there is still the question of whether a T+2 or T+3 deadline should be used for rolling settlements. The FBF agrees that this issue should be looked at in terms of costs and benefits, and therefore has no arguments in principle against carrying out this type of evaluation in order to assess whether there is a business case for the deadline, but requests that all market participants (including custodians) be involved.

**Key elements 4 and 5:** the FBF would like to point out that standard 3 should specify a standard maximum period for recycling failed transactions, and that a common rule should be applied at the end of the recycling period to deal with instructions that are still outstanding.

**Key element 6:** the main difficulty the FBF can see with settlement timetables is ensuring they are compatible with timetables for handling batch trades. Consequently, we think it would be preferable if the standard were to focus on two issues: setting timetables for settlements which are sufficiently broad (both at night and during the day), and ensuring a sufficiently high daily frequency of batch processings.

As regards the addressees, this standard should indeed be aimed at all market participants and associated operators.



***Standard 4 : Central Counterparties (CCPs)***

***The benefits and costs of a CCP should be evaluated. Where such a mechanism is introduced, the CCP should rigorously control the risks it assumes.***

**Addressees : market participants and CCPs.**

***Response:***

The FBF is fully in favour of the development of CCPs, and their convergence into a single clearing and guarantee body.

**Key element 2:** indeed, the advantages of an autonomous CCP structure have largely been demonstrated and in some countries this is already standard practice for transactions on regulated markets. The use of a CCP has numerous and almost unquestionable advantages (limitation of risks, notably through netting procedures, reduction in own capital required to cover transactions, etc.). Of course, a CCP should only have one activity: clearing and guaranteeing orders. In this respect, it should not expose itself to any risks which are not fully guaranteed. With respect to the regulations, the FBF would suggest that CCPs be given a special status and regulated accordingly.

The FBF agrees with the proposed list of addressees.

***Standard 5 : Securities lending***

***Securities lending and borrowing (or repurchase agreements and other economically equivalent transactions) should be encouraged as a method for expediting the settlement of securities. Barriers that inhibit the practice of lending securities for this purpose should be removed. The arrangements for securities lending should be sound, safe and efficient.***

***Addressees : Entities providing securities lending services in connection with the securities settlement process, including CSDs, CCPs and custodians operating systemically important systems.***

***Response:***

The FBF is in favour of this proposal which aims to promote securities lending mechanisms. However, the FBF feels that this overall category, "securities lending and borrowing", covers various different issues which are not reflected in the proposed standard. Furthermore, for the purpose of clarification, the standard needs to distinguish between the different participants likely to be concerned: all custodians need to be taken into account, then SSS operators which incur banking risks (ICSDs), and SSS operators which manage technical systems for securities borrowing and lending but do not incur credit risk (CSDs).

**Key element 8: the custodians.** Regardless of their size, their business is to offer banking services to their clients, subject to local banking regulations. With respect to the settlement of securities transactions, the standard should specify that all custodians must make every effort to anticipate any possible failures on the part of their clients and allow them to borrow the securities they require in order to avoid repercussions down the chain of settlements. The custodian can also grant clients holding securities access to liquidity under favourable conditions.

**Key elements 2, 4 and 5: SSS operators which do not expose themselves to credit risks (CSD).** These should only have an accounting role (a sort of notary for the circulation of securities). Their contribution should be restricted to the development, in conjunction with market participants (CCPs, Custodians and Investment Companies) of technical facilities for securities borrowing and lending and repos for securities borrowers which help to avoid or limit SSS failures for custodians. The standard should clearly specify that the facilities are not intended to transfer responsibility for the efficiency of settlements from the custodian to the CSD, but are to be used as a last resort to avoid outstanding suspense accounts. In this role as operator, the CSDs should never have to assume any part of the risk incurred by the lender vis à vis the borrower. The CSDs should leave the banking pools to bear the credit risk on borrowers. This ban on CSDs' exposure to credit risk is the very basis for the security of any settlement system.



**Key element 7:** in the case of ICSDs, insofar as they offer securities lending/borrowing services to the users of their SSS and incur credit risks, the FBF approves of the standard which aims to oblige them to take all appropriate security measures.

Conclusion: this standard should only apply to ICSDs.

***Standard 6 : Central securities depositories (CSDs)***

***Securities should be immobilised or dematerialised and transferred by book entry in CSDs to the greatest extent possible. To safeguard the integrity of securities issues and the interests of investors, the CSD should ensure that the issue, holding and transfer of securities are conducted in an adequate and proper manner.***

***In order to minimise systemic risks, CSDs should avoid taking risks to the greatest practicable extent.***

***Addressees : CSDs and registrars insofar as these entities perform for the function of securities issuance, the management of the issue and the transfer of securities through book entry.***

***Response:***

Overall, the FBF agrees with this standard but reiterates its firm opposition to risk-taking by CSDs.

**Key element 1:** the FBF is of course favourable to the dematerialisation of securities, to a central custodian and to the transfer of securities by book entry only and, finally, to the centralised management of securities issues which are, by nature, the responsibility of the CSDs and ICSDs under their notary role.

**Key element 3:** the FBF is in agreement with the principle expressed in the standard, that transactions should be handled by the CSDs and ICSDs under their notary role, using sound accounting standards. However, it feels that this would be insufficient if the CSDs, and other SSS operators (ICSDs), are not governed by a body of specifications containing a minimum of common accounting and operational obligations (see standard 1).

**Key element 4:** with respect to risks, the FBF restates its opposition to CSDs taking liquidity, market and counterparty risks. They should, however, take all necessary measures to eliminate or cover their operational risks.

***Standard 7: Delivery versus payment (DVP)***

***Principal risk should be eliminated by linking securities transfers to funds transfers in a way that achieves actual delivery versus payment.***

**Addressees : CSDs and custodians that operate systemically important systems.**

***Response:***

On the whole, the FBF is in agreement with this standard.

**Key element 3:** the FBF is, of course, in favour of the general application of the DVP principle, even if it is impossible to eliminate all securities transfers without counter transfers in cash for certain transactions (e.g. transfers of securities portfolios between two custodians).

However, as there are various forms of DVP, it would be advisable to harmonise them as soon as possible, notably to enhance system interoperability for cross-border transactions. The FBF feels that the current lack of harmonised DVP processing is one of the main obstacles to the cross-border transfer of securities and thus to the creation of a domestic zone within the European Union.

**Another key element for the FBF:** as the use of central bank money provides the best guarantee for the security of DVP processing, it should be compulsory for all settlements, both for domestic (one SSS) and cross-border transactions (two SSSs).

This standard should be intended only for participants with notary activities.

***Standard 8 : Timing of settlement finality***

***Intraday finality should be provided through real-time or multiple batch processing in order to reduce risks and allow effective settlement across systems.***

**Addressees : CSDs and custodians that operate systemically important systems.**

***Response:***

In principle, the FBF is in agreement with this standard and refers to its comments on standards 3 and 7. It suggests that standards 3, 7 and 8 be merged and notes, furthermore, that they fall more under the realm of market practices than of regulatory standards.

**Key element 3:** we feel the SSSs should combine both types of settlement processing. Indeed, real-time and multiple batch processing should co-exist within an SSS, due to their specific advantages and complementarities. Hence our preference for a slight modification in the drafting of the 1st line ("real-time" and/or "multiple batch"). The FBF points out that every effort must be made to maintain a balance between batch and real-time processing to take advantage of the efficiency and irrevocability of real-time processing and of the efficiency of payment clearing in batch processing.

**Another key element for the FBF:** it is vital that the principle of irrevocability be applied to orders and transfers of funds and securities (domestic and cross-border transactions).

The standard should be for participants with notary activities.

***Standard 9 : Risk controls in systematically important systems***

***Entities that operate systemically important systems need to put in place rigorous risk control measures in order to ensure that the probability of failing to provide timely settlement is negligible. Systemically important systems that extend explicit credit to participants should employ robust risk mitigation measures and, whenever practicable, full collateralisation should be applied. Incomplete collateralisation must be complemented by additional risk mitigation measures such as minimum credit quality of the borrower, credit exposure limits and, on the part of the operator, an adequate minimum capital base and adequate internal risk control measures.***

***Operators of net settlement systems should institute risk controls that, at a minimum, ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle.***

***Addressees : CSDs and custodians that operate systemically important systems and who extend credit explicitly to their participants. It is also addressed to operators of settlement systems that net the obligations arising among their participants and thereby generate implicit credit exposures.***

***Response:***

The FBF reiterates its agreement with the objective of enhancing the security of clearing and settlement systems, but also reiterates the need to differentiate between the participants on the basis of their activities.

**Key elements 1 and 2:** the FBF agrees that SSS operators which clear positions (securities and/or cash), must put in place, in collaboration with their users, adequate measures to cover a failure to settle by the largest debtor, but that these measures must be completely free of credit risk for operators carrying out notary activities, and the level of risk should always be verified by those actually incurring the risks ( e.g. the guarantee Fund).

**Key elements 3, 4, 5 and 6:** the FBF considers that this standard is in no way applicable to custodians whose banking risk is already governed by banking and prudential regulations.

In its current form, this standard only concerns ICSDs in their added value activities.



***Standard 10 : Cash settlement assets***

***Assets used to settle payment obligations arising from securities transactions should carry little or no credit or liquidity risk. If central bank money is not used, steps must be taken to protect the participants in the system from potential losses and liquidity pressures arising from the failure of the cash settlement agent whose assets are used for that purpose.***

***Addressees : CSDs and custodians that operate systemically important systems and, more specifically, the cash payment arrangements for Settling securities transactions in their systems.***

***Response:***

The FBF has reservations on certain aspects of this standard:

**Key element 2:** the FBF considers that all CSDs "must" and not "should" offer a settlement service in central bank money. The objective of this standard is that central bank money be used as it has almost unlimited liquidity, and it will be easy to impose as the majority of the CSDs already do so.

**Key element 3:** CSDs must eliminate all settlements in commercial currencies due to the inherent risk they carry.

**Another key element for the FBF:** the entire chain of DVP settlement transactions between two SSSs (cross-border transactions) should be carried out in central bank money. However, where this is not the case – i.e. where one SSS operates in central bank money (CSD) and the other in commercial currency (ICSD) – this standard should impose specific security conditions for DVP transactions.

This standard therefore only concerns CSDs and ICSDs in the context of their notary activities.

***Standard 11 : Operational reliability***

***Sources of operational risk in the clearing and settlement process should be identified, monitored and regularly assessed. This risk should be minimised through the development of appropriate systems and effective controls and procedures. Systems and related functions should be (i) reliable and secure, (ii) based on sound technical solutions, (iii) developed and maintained in accordance with proven procedures, (iv) have adequate, scalable capacity and (v) have appropriate business continuity and disaster recovery arrangements that allow for timely recovery of operations and the completion of the settlement process.***

***Addressees : CSDs, CCPs and custodians that operate systemically important systems. For this standard to be effective, it also needs to be applied by other providers of services critical for clearing and settlement, such as trade confirmation, messaging services and network providers.***

***Response:***

On the whole, the FBF agrees with the contents of this standard

**Key elements 1 and 2:** the FBF fully approves of the principle of maximising operational security, particularly that of the infrastructure. Indeed, the operational risks of infrastructures (guarantee and notary activities) are potentially the most damaging and should therefore not only be controlled but also audited on a regular basis.

**Key elements 1 and 4:** the FBF points out that the operational risks incurred by added value activities are already covered by security procedures implemented by these establishments:

- in application of the regulations and standards,
- or in application of obligations, notably technical, imposed by the infrastructures,
- or as private initiatives in the context of the establishment's security policy and desire to enhance its competitive position (SLA).

Nonetheless, the FBF recognises the need for all custodians to ensure service continuity; this standard could therefore be envisaged, provided it is not made redundant by the other existing regulations on the subject (Basel II, etc.).

***Standard 12 : Protection of customers' securities***

***Entities holding securities in custody should employ accounting practices and safekeeping procedures that fully protect customers' securities. It is essential that customers' securities be protected against the claims of the creditors of all entities involved in the custody chain.***

***Addressees : Entities holding customers' securities accounts, including registrars, CSDs, CCPs and custodians.***

***Response:***

The FBF approves of the desire to regulate the activities of entities holding securities in custody in order to ultimately protect client assets (see standard 1). The FBF also points out that there is already a European regulation relating to guarantees of securities deposits (see directive 97/9 dated March 3, 1997 relating to the system for the compensation of investors).

***Standard 13 : Governance***

***Governance arrangements for entities providing securities clearing and settlement services should be designed to fulfil public interest requirements and to promote the objectives of owners and users.***

**Addressees : CSDs, CCPs and custodians with a dominant position in a particular market.**

***Response:***

The FBF recognises the importance of this standard but points out that the regulations should be fundamentally different depending on the addressee, i.e. they should depend on the activities carried out by the participants, as indicated in the introduction.

**Key element 1:** this standard cannot apply to custodians exercising added value activities or commercial companies which do not exclusively serve the general interests of the market.

On the contrary, this standard is vital for guarantee and notary activities (see our comments in the introduction): it should stress the fact that infrastructures must take into account the general interests of the market and users and must therefore respect the standards of governance specified in the "Company Law Action Plan", along with the criteria proposed by the Commission in its Green Paper on services of general interest.

**Standard 14 : Access**

*CSDs and CCPs and custodians with a dominant position in a particular market should have objective and publicly disclosed criteria for participation that permit fair and open access. Rules and requirements that restrict access should be aimed exclusively at the controlling of risk.*

**Addressees** : *CSDs CCPs and custodians with a dominant position in a particular market. For this standard to be effective, it also needs to be applied by other providers of securities services critical for clearing and settlement, such as trade confirmation, messaging services and network providers.*

**Response:**

In the FBF's view, this recommendation should be differentiated according to activity:

**Key element 3:** the FBF fully agrees that access to SSSs managed by public interest infrastructures must be authorised according to technical and public criteria.

On the other hand, the FBF feels that participants carrying out added value activities are entitled to base their client relationships on private and bilateral criteria, notably to minimise their risks.

**Key element 4:** the FBF also points out that competition laws applicable to financial intermediaries already prohibit any discriminatory practices or abuse of dominant positions.

In conclusion, this standard only appears relevant for notary activities.

***Standard 15 : Efficiency***

***While maintaining safe and secure operations, securities clearing and settlement systems should be cost—effective in meeting the requirements of users, including interoperability at both the national and the European level.***

***Addressees : CSDs, CCPs and custodians with a dominant position in a particular market. For this standard to be effective, it also needs to be applied by other providers of securities services critical for clearing and settlement, such as trade confirmation, messaging services and network providers.***

***Response:***

On the whole, the FBF agrees with this standard.

**Key elements 1 and 2:** however, it would like to stress the fact that infrastructures (CSDs and CCPs) must be vigilant over costs, but without jeopardising the security of their operations.

This standard must not be applied to participants with added value activities insofar as competitive pressures are already a major factor in ensuring efficiency.

**Key elements 3, 4 and 5:** the FBF supports the ESCB-CESR's objective of increasing the interoperability of SSS and harmonising systems and practices across the European Union. The definition and implementation of a European standard for DVP links between SSS seems to the FBF to be one of the main priorities for the heads of infrastructures.

Consequently, this standard should only apply to notary activities.

***Standard 16 : Communication procedures, messaging standards and straight-through processing***

***Entities providing securities clearing and settlement services and participants in their systems should use or accommodate the relevant international communication procedures and messaging and reference data standards in order to facilitate efficient clearing and settlement across-system. This will promote straight-through processing (STP) across the entire securities transaction flow.***

***Service providers should move toward STP in order to help to achieve timely, sage and cost-effective securities processing, including confirmation, matching, netting, settlement and custody.***

***Addressees : Entities providing securities clearing and settlement services, and participants. For this standard to be effective, it also needs to be applied by other providers of securities communication services, such as messaging services and network providers.***

***Response:***

The FBF agrees with the recommendations in this standard, the contents of which are already suggested in the "Giovannini" reports.



***Standard 17 : Transparency***

***CSDs, CCPs and custodians with a dominant position in a particular market should provide market participants with sufficient information for them to identify and evaluate accurately the risks and costs associated with securities clearing and settlement services.***

***Addressees : CSDs, CCPs and custodians with a dominant position in a particular market. For this standard to be effective, it also needs to be applied by other providers of securities services, such as trade confirmation services, messaging services and network providers.***

***Response:***

The FBF agrees with the general objective of transparency described in this standard but has the following reservations:

**Key elements 1 to 7:** the FBF thinks that it applies perfectly to market infrastructures, notably for the services and tariffs they offer. However, this standard is not applicable to custodians who, under banking regulations, already have to provide various reports, and will have to provide more under the Basel II regulations.

This standard should therefore only apply to participants with notary and guarantee activities.

***Standard 18 : Regulation, supervision and oversight***

***Entities providing securities clearing and settlement services should be subject to transparent, consistent and effective regulation, supervision and oversight. Central banks and securities regulators/supervisors/overseers should co-operate with each other and with other relevant authorities, both nationally and across borders (in particular within the European Union), in a transparent manner.***

***Addressees : Central banks, securities regulators and, where appropriate, banking supervisors.***

***Response:***

On the whole, the FBF agrees with the contents of this standard.

**Key elements 1 to 6:** the FBF is fully in favour of European cooperation in harmonising rules and controls for post-trading activities.

**Another key element for the FBF:** the FBF also wants to see post-trading activities recognised as investment services and granted a European passport.

***Standard 19 : Risks in cross-system links<sup>4</sup>***

***CSDs that establish links to settle cross-system trades should design and operate such links to effectively reduce the risks associated with cross-system settlements.***

***Addressees : CSDs and custodians operating systemically important systems that establish cross-system links.***

***Response:***

The FBF is fully aware of the importance of this standard and reiterates its firm position on the role of the CSDs

**Key element 5:** as CSDs are not supposed to bear credit risk, the FBF is completely opposed to their incurring credit risks on each other via cross-system settlements.

**Key element 6:** in the case of relayed links, the FBF is fully aware that the length of these cross-system links (i.e. the number of systems in the chain for a cross-border settlement) is a potentially serious risk factor, and requests that the standard specify, on the one hand, that relayed links must be as short as possible and, on the other hand, that the role of custodians in these relayed links be restricted to that of technical operator.

**Another key element for the FBF:** the FBF is in favour of the interoperability of SSS but thinks this will only bring advantages in terms of costs and security if it is based on harmonised cross-border delivery procedures. This harmonisation must be carried out on the basis of standards 2 (Trade confirmation and settlement matching), 3 (Settlement cycles), 5 (Securities lending), 6 (Central securities depositories), 7 (Delivery versus payment, DVP), 8 (Timing of settlement finality), 10 (cash settlement asset).

In general, and in order to implement a truly domestic post-trading organisation in the European Union as quickly as possible, the FBF believes an "authority" should be established which would help speed up the interoperability of infrastructures.

This standard should only apply to notary activities.

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<sup>4</sup> This standard does not cover links established by CCPs. These will be covered by the future work of the ESCB-CESR on CCPs.