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| 18 December 2014 |

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| Reply form for the Technical Advice under the CSDR  |
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| Date: 18 December 2014 |

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA Consultation Paper - D Technical Advice under the CSDR, published on the ESMA website.

***Instructions***

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, please follow the instructions described below:

1. use this form and send your responses in Word format;
2. do not remove the tags of type <ESMA\_QUESTION\_TA\_CSDR\_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
3. if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

1. if they respond to the question stated;
2. contain a clear rationale, including on any related costs and benefits; and
3. describe any alternatives that ESMA should consider

**Naming protocol:**

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA\_ TA\_CSDR \_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

E.g. if the respondent were ESMA, the name of the reply form would be ESMA\_ TA\_CSDR \_ESMA\_REPLYFORM or ESMA\_CE\_AIFMD\_ESMA\_ANNEX1

To help you navigate this document more easily, bookmarks are available in “Navigation Pane” for Word 2010 and in “Document Map” for Word 2007.

Responses must reach us by **19 February 2015**.

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input/Consultations’.

***Publication of responses***

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

***Data protection***

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Disclaimer’.

# General information about respondent

|  |  |
| --- | --- |
| Are you representing an association? | No |
| Activity: | Other |
| Country/Region | Europe |

Q1: What are your views on the proposed basis for the cash penalty calculation?

<ESMA\_QUESTION\_TA\_CSDR\_1>

**T2S Advisory Group (AG) response to Q1**

***Section 2.1.1***

The T2S Advisory Group (AG) welcomes ESMA’s approach regarding the harmonisation principle for the calculation of penalties (i.e. by the usage of a single *reference price*).

However, there are issues regarding the required harmonisation/standardisation of the source, data, dates etc. of a harmonised reference price in the EU. If the EU CSD do not use a single source ensuring the standardisation of the reference price data, harmonisation and level playing field would not be possible for CSDs and their participants. See also AG comment on Q6 of the Consultation of ESMA on the Technical Standards under the CSD Regulation regarding the date reference of such reference price

<ESMA\_QUESTION\_TA\_CSDR\_1>

Q2: What are your views on the proposed approach regarding the categories of financial instruments and the penalty rates? In particular, do you consider that these penalty rates could dis-incentivise trading in small caps? Please provide evidence to support your views.

<ESMA\_QUESTION\_TA\_CSDR\_2>

**AG response to Q2**

***Section 2.1.2,***

***Paragraph 47:***

The AG would like to note that the ESMA proposed asset classification (e.g. separate category “corporate bonds”) is not in line with the ISO classification (i.e. ISO 10962 regarding the Classification of Financial Instruments -CFI code-).

See also AG response to Question 5 of the Consultation of ESMA on the Technical Standards under the CSD Regulation.

***Paragraph 52:***

The AG would like to underline that there are discrepancies between the RTS requirements on buy-ins and on those on penalties (as well as discrepancies between the different categories in this Technical Advice and the rest of the RTS).

For example, in RTS art. 4(2) d) *(of the system of monitoring fails)* the categories of financial instruments, to be differentiated (i.e. equities; fixed-income; exchange-traded funds (ETFs); units in collective investment undertakings, other than ETFs; money-market instruments; emission allowances) are different from the ones included in the table for penalties under para 52 of this consultation. See also the AG response to Q5 of the Consultation of ESMA on the Technical Standards under the CSD Regulation regarding the RTS on Settlement discipline Art. 4(2)(d).

Finally, the T2S AG would invite ESMA to provide further clarity on i) which penalty and ii) from which party the penalties should be charged in the following cases:

a) in the case the reasons of a fail are both “lack of securities” and “lack of cash”;

b) in the case in which one or both counterparties have put the instruction “on hold” (who pays the penalty to whom?)

The AG is inviting clarification on the penalties to be paid by the parties when the reason for the fail is that the settlement instruction is “on party/counterparty hold” based on our interpretation of the draft RTS on Settlement discipline Art. 7(1) *“The CSD shall calculate penalties for each settlement instruction that fails to settle, on the intended settlement date including for settlement instructions that are on hold.”*

The AG does not challenge that instructions set “on hold” by the counterparties should be subject to penalties. However, the AG would invite ESMA to consider whether instructions set on hold by market infrastructures (i.e. CSDs and CCPs) should be exempted from the penalty regime. The AG is of the opinion that there are important reasons why an infrastructure may set instructions on hold and these reasons are not for circumventing the penalty regime:

a) pending validation process;

b) temporary blocking of settlement which is pending on payment of the cash related to the transaction (possibly cash payment outside the settlement system);

c) instructions on hold due to buyer protection (see AG response to Q3 below);

d) a CSD is asked to implement some restrictive court order, etc.

<ESMA\_QUESTION\_TA\_CSDR\_2>

Q3: What are your views on the proposed approach regarding the increase and reduction of the basic penalty amount?

<ESMA\_QUESTION\_TA\_CSDR\_3>

**AG response to Q3**

***Section 2.2:***

The AG supports the view expressed by ESMA in paragraph 59 that for standard activity, and under standard circumstances, the system should be simple, and that no increase or decrease should be used.

In paragraph 60, ESMA provides some examples of situations when the penalty could be reduced to zero. The AG would like to express its support for this approach. However, the AG would like to ask ESMA to provide clearer guidance on the exact cases where the penalty rate can be reduced to zero. A harmonised approach on this policy would exclude that different markets follow their own rules resulting in a non-level playing field in the EU and possibly in regulatory arbitrage.

Furthermore, from the point of view of necessary IT developments to implement the cash penalties regime, there needs to be absolute clarity, across all EU CSDs, on the exact cases when the cash penalties should be applied.

In this respect, the AG would like to propose to ESMA that penalties should be charged only for fails with a fail reason “Lack of securities”, “Lack of cash” and “Settlement instructions on party/counterparty hold”; on all other fails, penalties on instructions should not be charged. This proposal has the benefit that it will provide clarity to CSDs for implementing initially a simplified cash penalties regime, which is easier to implement in practice. Such a simplified initial approach does not prevent ESMA from extending the cash penalties to failing instructions, which fail for other reasons at a later stage if it considers that this limited scope of reasons for fails is abused by the CSD participants. In particular, there are currently almost 20 standard ISO reasons codes *(see our reply to Q23 of Consultation on RTS on CSDR)* that are used to identify the reason a transaction is failing and there are multiple codes which are provided in certain cases. In each case there should be enough guidance from ESMA for each reason:

1) what penalty rate should be applied

and

2) which party to the transaction should be charged.

While these are straightforward and covered by ESMA for the separate reasons “Lack of securities” and “Lack of cash” in the table provided in para 52, no such information is provided for the other cases of the same table. In particular, information is lacking on who should be charged with what amount in case the instruction is “on party hold”. (see AG response to Q2 above).

Finally, ESMA could provide further clarifications in the cases of pending instructions put “on hold” by CSDs/CCPs on which “buyer protection” has been exercised. A buyer protection reflects the buyer’s choice of proceeds (on a pending transaction related to an optional corporate action) where the buyer has not yet received the securities on his account. The AG is of the opinion that when settlement instructions are put “on hold” as a result of buyer protection rules by CSDs or CCPs, no penalties should apply on such instructions “on hold”. This is because a pending instruction subject to buyer protection will eventually be cancelled by the CSDs/CCPs and converted into one or more new instructions by the CSD/CCP (in accordance with the EU corporate action standards).

<ESMA\_QUESTION\_TA\_CSDR\_3>

Q4: What are your views on the proposed approach regarding the cash penalties in the context of chains of interdependent transactions?

<ESMA\_QUESTION\_TA\_CSDR\_4>

**AG response to Q4**

The T2S AG could not identify how “chains of interdependent (settlement) transactions”, whatever the exact definition of such term could entail, could be identified by a CSD. The view of the AG is that in a framework of fungible book entry securities, identifying chains of individual and interdependent transactions is not possible, neither domestically nor cross-border. There can be a multitude of identical settlement transactions in a settlement engine and, in the absence of an additional and time consuming information flows from the custodian chain, no CSD is in a position to identify the business connection of these transactions. The AG understands that ESMA implicitly recognises this issue by proposing as a workaround solution the management of the distribution mechanism at the settlement level. See also the AG comments on Q7 on the Technical Standards regarding Art. 11(10) of RTS on settlement discipline.

Some AG members raised the point that when partial settlement is done, there are quantity thresholds that are applied. In certain cases, this may result in impeding the “immunization principle” (see ESMA’s Consultation paper on the Technical Advice para 61-63), which could be particularly problematic when a CCP is involved in the transaction chain.

<ESMA\_QUESTION\_TA\_CSDR\_4>

Q5: Do you agree with the proposed frequency of one year for the assessment of the substantial importance of a CSD in another Member State?

<ESMA\_QUESTION\_TA\_CSDR\_5>

The T2S Advisory Group (AG) considers the scope of this question as not directly relevant for T2S.

<ESMA\_QUESTION\_TA\_CSDR\_5>

Q6: What are your views on the proposed indicators?

<ESMA\_QUESTION\_TA\_CSDR\_6>

The T2S Advisory Group (AG) considers the scope of this question as not directly relevant for T2S.

<ESMA\_QUESTION\_TA\_CSDR\_6>

Q7: What are your views on the proposed thresholds?

<ESMA\_QUESTION\_TA\_CSDR\_7>

The T2S Advisory Group (AG) considers the scope of this question as not directly relevant for T2S.

<ESMA\_QUESTION\_TA\_CSDR\_7>

Q8: Do you believe that the proposed indicators and thresholds are relevant in the case of government bonds? If not, please provide details and arguments.

<ESMA\_QUESTION\_TA\_CSDR\_8>

The T2S Advisory Group (AG) considers the scope of this question as not directly relevant for T2S.

<ESMA\_QUESTION\_TA\_CSDR\_8>