Reply form

**on the** **call for evidence on shortening of the settlement cycle**

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

* respond to the question stated;
* indicate the specific question to which the comment relates;
* contain a clear rationale; and
* describe any alternatives ESMA should consider.

ESMA will consider all comments received by **15 December 2023.**

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

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

• Insert your responses to the questions in the Consultation Paper in this reply form.

• Please do not remove tags of the type < ESMA\_QUESTION\_SETT\_0>. Your response to each question has to be framed by the two tags corresponding to the question.

• If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.

• When you have drafted your responses, save the reply form according to the following convention: ESMA\_CP1\_SETT \_nameofrespondent.

 For example, for a respondent named ABCD, the reply form would be saved with the following name: ESMA\_CP1\_SETT \_ABCD.

• Upload the Word reply form containing your responses to ESMA’s website (**pdf documents will not be considered except for annexes**). All contributions should be submitted online at *www.esma.europa.eu* under the heading *‘Your input - Consultations’.*

**Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. 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 not to disclose the response 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 ‘[Data protection](https://www.esma.europa.eu/about-esma/data-protection)’.

**Who should read this paper?**

All interested stakeholders are invited to respond to this consultation paper. In particular, ESMA invites market infrastructures (CSDs, CCPs, trading venues), their members and participants, other investment firms, issuers, fund managers, retail and wholesale investors, and their representatives to provide their views to the questions asked in this paper.

# General information about respondent

|  |  |
| --- | --- |
| Name of the company / organisation | Association of German Public Banks |
| Activity | Associations, professional bodies, industry representatives |
| Are you representing an association? |[x]
| Country / Region | Germany |

# Questions

1. : Please describe the impacts on the processes and operations from compressing the intended settlement date to T+1 and to T+0. Please:
2. provide as much detail as possible on what issues would emerge in both cases and how they could be addressed with special attention to critical processes (matching, allocation, affirmation and confirmation) and interdependencies. Where relevant please explain if these are general or asset class/instrument/ trade specific.
3. Identify processes, operations or types of transaction or financial instrument class that would be severely impacted or no longer doable in a T+1 and in a T+0 environment.

**Please, suggest if there are legislative or regulatory actions that would help address the problems. Where relevant please explain if these are general or asset class/instrument/ trade specific.**

<ESMA\_QUESTION\_SETT\_1>

Please note, that we have answered the Call for Evidence mainly from the perspective of a change to T+1. As regards our position to T+0, please refer to the paper with the title “**ESMA Call for Evidence on Shortening the Settlement Cycle: High-Level Remarks of the European T+1 Industry Task Force**” that has been drawn up by numerous European and international associations, including namely EAPB and EBF of which we are member. This paper was submitted to ESMA on 14 December 2023.

We, the Association of German Public Banks, representing 63 public banks and approximately one-third of the German banking market, (including Landesbanken and promotional banks (Förderbanken)), fully support the work of the European institutions aimed at bringing benefits in terms of increased efficiency to securities settlement in the European Union. However, the increased operational costs and the operational risks that come along with a shortening of the settlement cycle must strike a balance with possible benefits in international cross-border business to which we as an association with members some of which operate only nationally do not attach overriding importance.

In addition to the considerations set out by ESMA in items 14 and 16 of the Call for Evidence, we would like to emphasise the following:

* Manual processes

Currently delays in the allocation and confirmation process often stem from manual processes. Certain market participants persist in utilizing email or voice communication for the transmission of allocation and confirmation details. The key factors contributing to pre-settlement matching issues are workflows involving manual interventions, dealer-to-custodian activities, and the behaviour of specific firms.

* Matching/confirmation/allocation processes

The market may need to accommodate to increasingly longer working days that would be required to finalise the matching process on trade date. The current architecture is not optimised to perform instruction, allocation, and confirmation under a reduced timeframe.

Irrespective of the manual processes, some settlement matching will inevitably move to settlement date. This can have implications for the timely settlement of back-to-back transactions relying on the positions of instructions that match late on settlement date.

Furthermore, not all breaks identified in the allocation/confirmation process are resolved on T+0, sometimes being left until the next business day. Some matching issues are not identified until the instructions reach the CSD.

Furthermore, intermediated transactions often lead to two different types of settlement: those between the custodian and a clearing member (client legs) and those between the clearing member and the CCP (market legs). For an ideal settlement, all these settlements should be processed at the same time (ie during the night settlement – NTS). This is achieved (more or less) today in a T+2 model. In a T+1 model, should the allocation / confirmation not be completed early enough to allow the custodian to instruct against the clearing member then the NTS will only process the already matched instructions sent by the CCP.

The business day in between trading and settlement to allow for processing of any manual or late bookings, or resolution of any mismatches will be lost, since the settlement window actually starts a few hours after the closing of the markets. Setting up a robust pre-settlement matching process would be of utmost importance.

* Confirmation standards and matching platforms

The establishment of market-wide confirmation standards or even a matching platform, similar to MarkitWire for derivatives, is imperative. This would streamline and standardize the confirmation processes across the market, enhancing efficiency and reducing operational risks. In essence, market-wide confirmation standards would entail agreed-upon protocols and procedures for confirming trades. This standardization ensures a consistent and transparent approach, reducing the likelihood of errors, discrepancies, and delays in the confirmation process. By implementing a matching platform, counterparties can automate the confirmation of trades, promoting a seamless and error-free exchange of information. Platforms like MarkitWire have demonstrated success in improving efficiency and reducing operational risks in derivative markets. Extending similar platforms or standards to a broader market scope would not only enhance the speed and accuracy of trade confirmations but also contribute to overall market integrity and stability. The establishment of such frameworks is a proactive measure to address challenges associated with manual confirmation processes and promote a more technologically advanced and efficient trading environment.

Important: Even if the confirmation process can be automated as far as possible, the resolution of discrepancies in the confirmations will remain a manual process (coordination between broker, service providers, back-office units or between traders). It will be a time challenge to ensure the clarification of differences on the trading day. It will probably only be possible to ensure this by means of the aforementioned longer attendance times in the back office and in trading.

However, the adoption of an allocation and confirmation platform might be excessively expensive for smaller buy-side entities, encompassing both implementation and ongoing operational costs. Furthermore, it is not clear how many systems will be used in the market for the implementation of DLT technology. If factually only one system will emerge and the market will use such monopolist (who then could set prices at will) its might be less costly than in case of the use of various systems and the need to pay for the associated connections and licencing costs.

* Standardisation of Data

The provision or retrieval of counterparty master data on platforms, obtainable in standard formats (SWIFT once initiated such an effort with “KYC Registry”), is a crucial aspect of financial processes. Counterparty master data includes essential information about counterparties, such as legal entities and their details. When this data is made available or retrieved from platforms in standardized formats, it facilitates seamless integration and compatibility across different systems. Standardization in data formats enhances interoperability and reduces the complexities associated with data integration. By adopting standardized formats, financial institutions can optimize the efficiency of processes related to counterparty information. It not only streamlines data exchange but also mitigates the risk of errors and discrepancies that may arise when dealing with diverse data structures. This, in turn, contributes to the overall operational efficiency and reliability of financial transactions. The emphasis on standardization in counterparty master data is a proactive measure towards creating a more cohesive and interoperable financial ecosystem.

<ESMA\_QUESTION\_SETT\_1>

1. : What would be the consequences of a move to a shorter settlement cycle for (a) hedging practices (i.e. would it lead to increase pre-hedging practices?), (b) transactions with an FX component?

<ESMA\_QUESTION\_SETT\_2>

When the securities market transitions to T+1, the hedging and foreign exchange (FX) activities, along with the associated collateral for derivatives, will need to align with the shortened settlement period. Consequently, the challenges stemming from the move to T+1 in the securities business extend to impact other processes within the front office and market operations.

The shift to a T+1 settlement cycle requires synchronization across various facets of financial activities. Hedging strategies, crucial for managing risk exposure, and FX transactions, integral to international trade and investment, will need to adjust their timelines to accommodate the accelerated settlement period. Additionally, collateral management practices related to derivatives will be affected, as the collateralization process will need to align with the faster settlement cycle.

As a result, the challenges initially associated with T+1 in the securities domain extend beyond, influencing front office functions and market follow-up processes. The need for real-time or accelerated decision-making, enhanced operational efficiency, and the adaptation of existing systems and procedures become imperative across the broader spectrum of financial activities. This underscores the interconnected nature of various processes within the financial landscape when transitioning to a T+1 settlement model.

As regards FX funding, one of the main innovations brought to FX markets in the last 20 years, has been the growth of PvP (Payment versus Payment) settlement through the increased use of the CLS platform (Continuous Linked Settlement, is a specialized financial infrastructure group who operates a global multicurrency cash settlement system, known as the CLS System, which plays a critical role in the FX market). CLS is a widely used settlement service in the FX market, providing simultaneous payment-versus-payment settlement for various currencies, reducing settlement risk. Despite this positive development, challenges around FX settlement risk remain:

* Time zone related challenges: instructions come from different regions, with some coming very close to the CLS deadline.
* Furthermore, CLS does not support all currencies. If CLS can be used for only a fraction of FX transactions, market participants may resort more to bilateral agreements for FX transactions and this business will increase. This shift to bilateral arrangements has cascading effects on risk management. Limits, which act as safeguards to control exposures, may need to be re-evaluated and adjusted to accommodate the increased volume of bilateral transactions. Additionally, collateral management practices in bilateral agreements will see an uptick, as counterparties may seek to mitigate credit risk through collateralization.

<ESMA\_QUESTION\_SETT\_2>

1. : Which is your current rate of straight-through processing (STP ), in percentage of the number and of the volume of transactions broken down per type of transaction or per instrument as relevant? In case STP is used only for certain processes/operations, please identify them. Which are the anticipated challenges that you envisage in improving your current rate of STP?

<ESMA\_QUESTION\_SETT\_3>

Especially for small to medium-sized enterprises, the need to invest more in automation and technology than their business volume would normally justify poses a challenge. This raises the question of whether these companies might opt to withdraw as direct participants from the market. Consequently, the diversity within the market diminishes.

Small and medium-sized enterprises (SMEs) often face a dilemma where advancements in technology and automation are essential for staying competitive, but the associated costs may outweigh the benefits relative to their business scale. This financial strain could prompt these enterprises to reconsider their direct participation in the market, as the required investments may not align with their economic feasibility.

The potential withdrawal of SMEs as direct participants from the market carries broader implications, particularly in terms of market diversity. A decrease in the number of active participants can impact the richness of perspectives, trading dynamics, and overall vibrancy within the market. It underscores the importance of considering the accessibility and affordability of technological advancements to ensure a diverse and inclusive marketplace.

In addition, as regards the anticipated challenges, we would like to highlight the problem stemming from the absence of Straight Through Processing (STP) processes for Repo events, primarily due to the complexity associated with recording and mapping these events. Additionally, the challenge is compounded by the current market standards, where important information is typically communicated via free text in platforms such as Bloomberg. This issue becomes particularly evident in scenarios involving open trades, such as repo or loan transactions, where the lack of standardized processes and the reliance on free-text communication methods can hinder seamless and automated handling of these events.

<ESMA\_QUESTION\_SETT\_3>

1. : Please describe the impacts that, in your views, the shortening of the securities settlement cycle could have beyond post-trade processes, in particular on the functioning of markets (trading) and on the access of retail investors to financial markets. If you identify any negative impact, please identify the piece of legislation affected (MiFID II, MiFIR, Short Selling Regulation…) and elaborate on possible avenues to address it.

<ESMA\_QUESTION\_SETT\_4>

In contrast to the US, where there is only one CSD and CCP, European markets are fragmented with a large number of CSDs and CCPs acting across the different EU Member States. There is also very little harmonisation in terms of local rules (such as for example insolvency law, withholding tax etc.). Some instruments are settled on multiple CSDs, resulting in a complex settlement process, where often several settlements need to take place to reach the final counterparty of a trade in one single instrument.

Actually, Euroclear and Clearstream, as well as all interconnected Central Securities Depositories (CSDs), would have to ensure that ISINs (International Securities Identification Numbers) are fully and accurately present in terms of master data. The subsequent setup of security master data would no longer be feasible within the shortened available timeframe. Currently, the absence of complete security master data at Euroclear or Clearstream, for example, already serves as a cause for settlement failures. This emphasizes the critical importance of having comprehensive and accurate ISIN-related master data available in a timely manner within the CSDs. Failing to establish the necessary security master data in advance can lead to complications in settlement processes, potentially resulting in settlement failures.

Due to its complexity and fragmentation, a large number of procedures in EU markets are still manual, such as for example the stock loan recall process, and there is a limited window of opportunity to recall securities to enable their usage for an open transaction. Should the broader market move to T+1, this would mean that the stocks would need to be recalled already on T+0, which, given the manual process, would be a significant challenge.

Another challenge pointed out is the already late market close in Europe which is 5.30pm, with a large number of trades being executed late into the close. As a result, a move to T+1 would make it very challenging to receive and process late incoming trades for example from the US on/after US closing hours.

Also, trading hours in Europe are currently not entirely compatible with a T+1 settlement cycle even within Europe. Taking Germany as an example:

* Stock trading is possible until 10 PM (and in recent years, trading hours have been continually extended).
* The settlement process on Target2-Securities (T2S) for a settlement day begins as early as 8 PM on the preceding day.
* This means that for a trade conducted at, for instance, 9 PM, the settlement for T+1 has already been underway for one hour.
* Additionally, the European Central Bank (ECB) has advocated for settlement to occur overnight in recent years, aiming for as much to be settled by the next morning, further encouraged by lower prices during nighttime.
* This would no longer be feasible with T+1; processes and timelines would need major adjustment and modification.

Aa regards the coverage of short positions, the standard practice involves short sellers closing their positions a day before regular trading activities. This preemptive move is influenced by considerations related to the liquidity of the securities financing markets. Covering short positions may become more costly because there are only a limited number of entities (addresses) providing this service on a T+0 basis. Since there may be fewer buyers and sellers, this will make it more challenging to execute trades and potentially increase the costs associated with covering short positions. This scenario could potentially amplify the influence of major players or large entities, referred to as "addresses," granting them even greater pricing power in the market due to the reduced competition in this specific aspect of trading. This concentration of influence among a select few may impact the overall dynamics of short position coverings, leading to increased costs for those involved in such transactions.

<ESMA\_QUESTION\_SETT\_4>

1. : What would be the costs you would have to incur in order to implement the technology and operational changes required to work in a T+1 environment? And in a T+0 environment? Please differentiate between one-off costs and on-going costs, comparing the on-going costs of T+1 and T+0 to those in the current T+2 environment. Where relevant please explain if these are general or asset class/instrument/ trade specific.

<ESMA\_QUESTION\_SETT\_5>

The adjustment of current cut-off times at the (International) Central Securities Depositories ((I)CSDs), some of which are set at 4 PM, implies a potential ripple effect on the operational schedules downstream. Extended presence times in market operations, while accommodating adjusted cut-off times, could result in increased personnel costs. This is particularly noteworthy even as processes become more automated and efficient since the need for extended presence implies ongoing staffing requirements. This holds in particular also true for trading staff. They are needed at the long end to resolve unconfirmed transactions. As a consequence, this also means longer attendance times in the front office.

One factor are the general implementation costs – mainly IT. These IT costs are incurred to optimize processes, reduce settlement times, and enhance overall efficiency. While they are a necessary investment in the long-term improvement of operational workflows, the initial financial outlay for adapting infrastructure to Straight Through Processing (STP) is a distinct and upfront consideration for organizations within the financial industry. While implementing STP is a crucial step in enhancing operational efficiency and reducing manual intervention in financial processes. However, transitioning to STP involves initial investments in technology, software, and system upgrades, constituting one-time expenses.

In addition, the transition to a more technologically advanced infrastructure requires investments not only in initial setup but also in continuous updates. While the benefits of improved efficiency and automation are clear, the accompanying costs, both one-time and ongoing, present considerations that require careful evaluation and planning. The expected ongoing costs with each system release change make it challenging to precisely quantify the overall expenditure.

Another, ongoing cost factor – and which will, therefore, remain - are the higher liquidity costs that arise from the necessity to have more liquidity available within a shorter timeframe. This situation compels market participants to maintain increased liquidity reserves to accommodate the compressed timeframe for transactions, thereby incurring continuous expenses.

<ESMA\_QUESTION\_SETT\_5>

1. : In your view, by how much would settlement fails increase if T+1 would be required in the short, medium and long term? What about T+0? Please provide estimates where possible.

<ESMA\_QUESTION\_SETT\_6>

We would assume that also in the long term not every market participant will implement STP. Hence, settlement fails will increase in the beginning and due to inefficiencies in the processes will remain also in the long term. The occurrence of settlement failures is a current challenge stemming from the inconsistent availability of security master data across various entities involved in financial processes, including (I)CSDs. Inconsistent data among stakeholders can lead to discrepancies, errors, and ultimately result in settlement failures, where transactions are not successfully completed.

This underscores the critical importance of establishing standardized and synchronized processes for managing security master data throughout the entire lifecycle of financial transactions. Achieving a uniform and up-to-date dataset across all participants, including (I)CSDs, is essential to mitigate the risks associated with settlement failures, ensuring the smooth and efficient functioning of financial markets. Efforts toward enhancing data consistency and collaboration among process participants are essential in addressing this challenge and promoting a more reliable and robust financial infrastructure.

<ESMA\_QUESTION\_SETT\_6>

1. : In your opinion, would the increase in settlement fails/cash penalties remain permanent or would you expect settlement efficiency to come back to higher rates with time? Please elaborate.

<ESMA\_QUESTION\_SETT\_7>

We expect an increase in Late Matching Penalties under CSDR and additional costs and complexities of the missing overnight settlement batch, if there is no major improvement in processes. To some extent, we even expect them to remain permanent. Even in the long term, not every market participant will implement STP. Hence, settlement fails due to inefficiencies in the processes will remain.

A worse settlement rate could lead to further punitive CSDR measures from EU authorities (such as increased penalties or the introduction of mandatory buy-ins).

<ESMA\_QUESTION\_SETT\_7>

1. : Is there any other cost (in particular those resulting from potential impacts to trading identified in the previous section) that ESMA should take into consideration? If yes, please describe the type of cost and provide estimates.

<ESMA\_QUESTION\_SETT\_8>

Please refer to our answer under Question 5: An ongoing cost factor are the higher liquidity costs that arise from the necessity to have more liquidity available within a shorter timeframe. This situation compels market participants to maintain increased liquidity reserves to accommodate the compressed timeframe for transactions, thereby incurring continuous expenses.

Furthermore, it has to be kept in mind that additional costs (besides settlement fails and cash penalties) will arise due to the utilization of increased bilateral foreign exchange (FX) swaps. The associated costs arise particularly in terms of setting and managing limits. Bilateral FX swaps involve the exchange of currencies directly between two parties, and the costs associated with these transactions can include fees, spreads, and other expenses related to managing counterparty risk and market volatility.

Moreover, the requirement for additional collateral in the context of these transactions contributes to higher funding costs. Collateral is often used to mitigate credit risk, and an increase in collateral demands can impact overall funding expenses for the parties involved in the bilateral FX swaps.

<ESMA\_QUESTION\_SETT\_8>

1. : Do you agree with the mentioned benefits? Are there other benefits that should be accounted for in the assessment of an eventual shortening of the securities settlement cycle?

<ESMA\_QUESTION\_SETT\_9>

No, we do not fully agree with the mentioned benefit. Possibly lower collateral requirements may be outweighed by higher FX funding costs. Also being aligned with other jurisdictions is not a benefit for all market participants but rather only for the internationally active ones.

<ESMA\_QUESTION\_SETT\_9>

1. :Please quantify the expected savings from an eventual reduction of collateral requirements derived from T+1 and T+0 (for cleared transactions as well as for non-cleared transactions subject to margin requirements).

<ESMA\_QUESTION\_SETT\_10>

The EU market can be characterised as a non-cash collateral market, which means that banks and other institutions are providing collateral in asset form, which results in multiple settlements related to the same transaction. A move to T+1 would put further stress to this multi-settlement approach. A large part of borrowing activity is collateralised via tri-party agents. A move to T+1 would mean that those parties would be unable to move collateral without friction on a same day basis and will, therefore, likely resort to placing excess collateral at the tri-party agent. This will increase funding costs and potentially drain liquidity from other areas, disrupting the market for securities financing as a whole. Hence, we do not fully support the assumption that collateral requirements will be reduced and collateralisation itself will be even more challenging.

<ESMA\_QUESTION\_SETT\_10>

1. : If possible, please provide estimates of the benefits that you would expect from T+1 and from T+0, for example the on-going savings of potentially more automated processes.

<ESMA\_QUESTION\_SETT\_11>

A higher degree of automation and the increased use of standardised platforms may be advantageous at first glance. However, the respective implementation as well as maintenance and support are associated with (additional) costs. The cost-benefit calculation varies from institution to institution, depending on volume, product scope and the existence of customer business. Therefore, it is not possible to provide a general information about the possible benefits. As already formulated in the answer to Q3, the requirements may rather lead to a withdrawal of SME's as direct market partners because the costs and benefits are not worthwhile for these institutions.

<ESMA\_QUESTION\_SETT\_11>

1. : How do you assess the impact that a shorter settlement cycle could have on the liquidity for EU markets (from your perspective and for the market in general)? Please differentiate between T+1 and T+0 where possible.

<ESMA\_QUESTION\_SETT\_12>

A move to T+1 does mean a shorter window in which to access liquidity. This is especially an issue for trades that come late in the day, near market close. The costs associated with liquidity increase where there is a demand for readily available funds to meet financial obligations within a limited timeframe. Holding more liquidity is generally costly, as it often involves keeping a higher proportion of assets in cash or other easily tradable instruments.

As an example, since currently there are no real-time information flows between trading and funding desk and the repo desk, secured funding desks usually rely on overnight maturity transactions. In case of any operational disruption, there is a liquidity trap which might force a higher cash buffer maintenance, and which will hence increase the cost of business for banks and hence clients. If it came to T+1, banks would need to hold a larger amount of intraday liquidity as pre-funding needs will grow substantially due to faster settlement (ie from a trader’s perspective, one cannot simply wait until a trade “comes in” and instruct to settle at a later point; in a T+1 world the liquidity would need to be held already in anticipation of new trades). Hence, in a T+1 settlement world, the repo market may evolve into a T+0 market. Such factual transition to a T+0 settlement model in the repo market can influence bid/ask spreads, a crucial aspect of market dynamics. In a T+0 environment, where settlement occurs almost immediately, the bid/ask spreads may experience changes, potentially impacting the profitability and risk management strategies of market makers. The immediacy of settlement in a T+0 setting can introduce challenges for market participants in terms of pricing and managing liquidity.

In terms of trading activity, there are reasons to believe that there will be a decreased trading activity/ provision of liquidity from market makers in those instruments which would be hard to find in the repo market. Possible transactions to think about here would be the offering of an illiquid corporate or High Yield bond for example, or, on the Equity side, arbitrage option strategies again involving shorting cash instruments such as shares. Whereas T+2 allowed the trading side 1 day to source the relevant instrument(s), a move to T+1 would mean those had to be sourced on T+0. As a result, higher bid-offer spreads in, or even the non-offering of those instruments, could be expected, and/or a decreased activity or a general forced change in option trading strategies.

Furthermore, the higher volume of transactions at T+0 on platforms like Eurex/LCH can lead to an increase in intra-day margin requirements. This, in turn, may result in higher liquidity demands as market participants need to allocate additional funds to meet these margin requirements, ultimately leading to increased costs.

In summary, the shift to a T+1 settlement can have profound effects on the repo market, on bid/ask spreads and may pose challenges to market makers in terms of liquidity provision. Additionally, the surge in transaction volume at T+0 can trigger higher intra-day margin requirements, potentially amplifying liquidity needs and associated costs for market participants.

<ESMA\_QUESTION\_SETT\_12>

1. : What would be the benefits for retail clients?

<ESMA\_QUESTION\_SETT\_13>

Retail customers are also facing new demands on their liquidity planning. If retail customers also switch to T+1, they would have to provide their liquidity one day earlier when making a purchase. On the other hand, customers receive their liquidity sooner when selling. There are no significant advantages.

<ESMA\_QUESTION\_SETT\_13>

1. : How would you weigh the benefits against the costs of moving to a shorter settlement cycle? Please differentiate between a potential move to T+1 and to T+0.

<ESMA\_QUESTION\_SETT\_14>

While the reduction to a T+1 settlement cycle may seem advantageous in terms of expediting processes, it introduces a host of challenges and associated costs. These challenges extend beyond the immediate securities market, affecting derivative transactions and funding activities. The need for real-time or accelerated processing may necessitate substantial adjustments to existing systems and practices, incurring both direct and indirect costs.

A notable concern is that smaller financial institutions may opt to withdraw from the market due to the increased burden, leaving only a few larger institutions active. This potential outcome contributes to a diminishing market diversity, as the complexity and costs associated with transitioning to T+1 settlement may disproportionately impact smaller players. The overarching effect is a potential reduction in the richness of perspectives, competition, and overall vibrancy within the financial market.

Overall, the disadvantages (costs and efforts, loss of market diversity and new risks) appear to outweigh the advantages (higher degree of automation, possible reduction of credit risks from today's perspective and based on current knowledge of the situation.

<ESMA\_QUESTION\_SETT\_14>

1. : Please describe the main steps that you would envisage to achieve an eventual shorter securities settlement cycle. In particular, specify: (i) the regulatory and industry milestones; and (ii) the time needed for each milestone and the proposed ultimate deadline.

<ESMA\_QUESTION\_SETT\_15>

From our point of view, an increase in the usage and data quality of SSI platforms is essential. Furthermore, trades would need to exhibit greater sensitivity when entering trades, particularly with regard to the settlement location or counterparty entity, especially when in a cross-border context multiple entities may be involved.

To enhance operational efficiency and promote a synchronized financial ecosystem, industry-wide adjustments would be necessary. Firstly, there is a call for coordinated CSD opening hours on a pan-European level, fostering alignment in the timing of securities settlement activities. This coordination aims to streamline cross-border transactions and ensure a cohesive approach to market operations.

The extension of intraday settlement processing windows allows for a more flexible timeframe within which settlement activities can occur. This adjustment caters to the dynamic nature of financial markets and accommodates varying needs across different time zones and market participants.

Similarly, the extension of ECB/T2 opening hours contributes to the overall flexibility and accessibility of settlement services, aligning with the goal of facilitating smoother and more efficient transactions.

Lastly, the implementation of electronic over-the-counter (OTC) standard confirmations signifies a move towards digitization and automation in the confirmation process for OTC transactions. This not only enhances operational efficiency but also reduces the risk of errors associated with manual confirmation processes.

These industry-wide adjustments are collectively necessary in order to improve the efficiency, transparency, and resilience of financial market operations, fostering a more integrated and technologically advanced landscape.

<ESMA\_QUESTION\_SETT\_15>

1. : Assuming that the EU institutions would decide to shorten the securities settlement cycle in the EU, how long would you need to adapt to the new settlement cycle? And in the case of a move to T+0?

<ESMA\_QUESTION\_SETT\_16>

At least 18 months.

<ESMA\_QUESTION\_SETT\_16>

1. : Do you think that the CSDR scope of financial instruments is adequate for a shorter settlement cycle? If not, what would be in your views a more adequate scope?

<ESMA\_QUESTION\_SETT\_17>

Only instructions originating from trading venue transactions (Regular Markets, MTF, or OTF) should be in scope.

<ESMA\_QUESTION\_SETT\_17>

1. : Is it feasible to have different settlement cycles across different instruments? Which are the ones that would benefit most? Which least?

<ESMA\_QUESTION\_SETT\_18>

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<ESMA\_QUESTION\_SETT\_18>

1. : Which financial instruments/ transaction types are easier to migrate to a shorter settlement period in the EU capital markets? Does the answer differ by asset class? Should it be feasible/advisable to have different migration times for different products/markets/assets? If yes, please elaborate.

<ESMA\_QUESTION\_SETT\_19>

We would assume that primary market transactions are out of scope as well as transactions not involving two trading parties, such as, securities account transfers or free of payment transactions in the (de)mobilisation of collateral.

There will be additional challenges for loans and repos for which more information must be included on allocations / confirmations (e.g. rate, maturity,…).

Also instruments on which the final price is dependent on overnight price feeds – e.g. ETF creation and redemptions or listed derivatives – will be strongly affected by the migration to a shorter settlement cycle.

Furthermore, trading in certain derivative instruments might become more difficult, such as for example in the case of options. At this point in time, the software containing pricing models for stock option trading allows for T+2 settlement in most products. Such software would need to be adjusted or would result in different manual adjustments of valuations by traders, which would affect their pricing of the product. Software providers should be able to accommodate for the change, but this will come at a cost.

<ESMA\_QUESTION\_SETT\_19>

1. : Do you think that the settlement cycle for transactions currently excluded by Article 5 of CSDR should be regulated? If you think that the settlement cycle of some or all of these transactions should be regulated, what would be in your view an appropriate length for their settlement cycle?

<ESMA\_QUESTION\_SETT\_20>

No. OTC securities transactions are already being settled with T+2, although the CSDR only prescribes T+2 for exchange-traded transactions. The OTC market therefore follows the trading venue business. It can be assumed that this will also be the case when settlement is shortened to T+1.

<ESMA\_QUESTION\_SETT\_20>

1. : Please describe the impact(s) that the transition to T+1 in other jurisdictions has had or will have on your operations, assuming the EU remains on a T+2 cycle.

<ESMA\_QUESTION\_SETT\_21>

The answer to this question depends on the scope of business of the respective institution. If the focus is on trading and settlement in the EU market, different settlement times between jurisdictions on a worldwide scale have very little effect.

If an institution is active in many markets and these prescribe different settlement times, then from an affirmation/confirmation & matching perspective, several separate workflows are required for differing settlement cycles. This may lead to confusion, namely for multi-listed securities, ADR and baskets with securities underlying coming from both geographies.

<ESMA\_QUESTION\_SETT\_21>

1. : Can you identify any EU legislative or regulatory action that would reduce the impact of the move to T+1 in third countries for EU market participants? Please specify the content of the regulatory action and justify why it would be necessary. In particular, please clarify whether those regulatory actions would be necessary in the event of a transition of the EU to a shorter settlement cycle, or they would be specific only to address the misaligned cycles.

<ESMA\_QUESTION\_SETT\_22>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_SETT\_22>

1. : Do you see benefits in the harmonisation of settlement cycles with other non-EU jurisdictions?

<ESMA\_QUESTION\_SETT\_23>

For market participants acting on a global level, being synchronised with those markets helps to enable standardisation and coverage models. For smaller market participants not acting on a global level there is no merit in harmonising settlement cycles with other non-EU jurisdictions.

<ESMA\_QUESTION\_SETT\_23>

1. : Would reducing the settlement cycle bring any other indirect benefits to the Capital Markets Union and the EU's position internationally?

<ESMA\_QUESTION\_SETT\_24>

Based on current knowledge, no further indirect benefits from the reduction of the settlement cycle are recognisable.

<ESMA\_QUESTION\_SETT\_24>

1. : Do you consider that the adaptation of EU market participants to the shorter settlement cycles in other jurisdictions could facilitate the adoption of T+1 or T+0 in the EU? Please elaborate.

<ESMA\_QUESTION\_SETT\_25>

Not in all circumstances. There are many EU market participants who do not have any settlement outside of the EU. For them, a move to T+1 in the EU will be something completely new to implement.

<ESMA\_QUESTION\_SETT\_25>

1. : Would different settlement cycles in the EU and other non-EU jurisdictions be a viable option?

<ESMA\_QUESTION\_SETT\_26>

It is difficult to foresee, whether probably reduced collateral requirements are actually a factor for increasing the attractiveness of the relevant market. In particular, since this reduction on the one hand might be outweighed by FX funding issues.

Furthermore, remaining on T+2 would mean that the amount of settlement fails would not negatively be impacted, since the current available settlement window is much more amenable to reducing errors, resolving mismatches and avoiding fails. Greater penalties are therefore avoided. There would also be cost savings as market participants would not be required to update systems and change processes.

While it is best not to be reactive but proactive and be prepared to adequately roll out any new framework the EU intends to implement, we recommend to take the time to learn from US lessons once their T+1 system is in place. We are of the view that this will make it easier to identify any necessary changes to legislation.

<ESMA\_QUESTION\_SETT\_26>

1. : Please elaborate about any other issue in relation to the shortening of the securities settlement cycle in the EU or in third-country jurisdictions not previously addressed in the Call for Evidence.

<ESMA\_QUESTION\_SETT\_27>

In assessing the overall impact of transitioning to a new settlement cycle, it's crucial to consider not only the potential capital savings but also the comprehensive set of process-related costs that may arise during and after the implementation of the new settlement framework.

While there is a possibility of realizing capital savings, it's important to consider the associated process costs that may mitigate these potential gains. Extended presence times, possibly required for adapting to a new settlement cycle, can result in increased labor costs. Additionally, the transition may necessitate higher IT expenses for system modifications or upgrades to accommodate the new settlement timeframe.

Moreover, the potential for errors due to time constraints is a notable concern. Rushed processes can lead to mistakes and inefficiencies, resulting in additional costs associated with error resolution and potential disruptions to the overall workflow.

Shortening the settlement cycle can also lead to a reassessment of IT recovery times and emergency processes. Today's IT restart times are geared towards T+2. In the "T+2 world", one day more is available to solve the IT problem in order to route securities instructions or payment orders to CSDs or T2 or correspondent banks. Under T+1, the restart times would have to be significantly shortened. Depending on the sensitivity of the IT system (e.g. payment transaction systems), the costs and effort required to place all orders in the market on time can be very high.

Finally, apart from any settlement considerations and processes, it should be kept in mind that even the onboarding of new clients will have less time to remediate initial teething issues. It will be factually impossible to onboard a new client and enter into a transaction that same day. This also applies to the onboarding of new customers in other product groups that must comply with the T+1 securities settlement (see also answer Q2).

<ESMA\_QUESTION\_SETT\_27>