Reply Form

**to the Consultation Paper on Technical Advice on the Scope of CSDR Settlement Discipline**

Responding to this Consultation Paper

ESMA invites comments on all matters in this Consultation 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 **9 September 2024.**

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\_SETD\_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\_ SETD\_nameofrespondent.

 For example, for a respondent named ABCD, the reply form would be saved with the following name: ESMA\_CP1\_ SETD\_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, credit institutions, 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 | Grupo BME |
| Activity | CSD |
| Are you representing an association? | ☐ |
| Country / Region | Spain |

# Questions

1. Do you agree with ESMA’s proposal regarding the underlying causes of settlement fails that are considered as not attributable to the participants in the transactions? Please specify which cases you agree with and which cases you don’t agree with (if applicable). Please justify your answer and provide examples and data where available.

<ESMA\_QUESTION\_SETD\_1>

Before answering to the question itself, we would like to mention some preliminar aspects:

* To kindly ask ESMA to consider sufficient lead time must be granted to all stakeholders so that their IT department can implement and enact any system changes.
* Considering the current practice applied by CSDs in line with the “ECSDA Penalties Framework”, we generally support ESMA proposal to focus on transactions and data that are truly relevant regarding settlement and financial risk aspects and specify settlement fails that are considered as “not attributable to the participants in the transactions”.

Regarding the underlying causes of settlement fails that are considered as not attributable to the participants in the transactions, most cases put forward by ESMA are already taken care of with the existing functionalities and / or operational framework in place, as detailed in the paragraphs below.

Four cases of exemptions were already outlined in [ESMA’s Q&As on the implementation of CSDR](https://www.esma.europa.eu/sites/default/files/library/esma70-708036281-2_csdr_qas.pdf) under answer a) of Settlement Discipline Questions 4 (Cash penalties: scope), i.e. :

a) ISIN suspension from settlement due to a reconciliation issue under Article 65 (2) and (6) of the RTS on CSD Requirements;

b) ISIN suspension from trading, such as for example under Article 32(1), Article 52(1), Article 69(2) of MiFID II or Article 40(1) of MiFIR;

c) settlement instructions involving cash settlement outside the securities settlement system operated by the CSD if, on the respective day, the relevant payment system is closed for settlement;

d) technical impossibilities at the CSD level that prevent settlement, such as: a failure of the infrastructure components, a cyber-attack, network problems, technical (IT) issues in the system of the CSD.

From an operational standpoint:

* Cases falling under a) and d) are already handled ex-post via the T2S penalty mechanism appeal process and subsequent removal request of cash penalties by the CSD. The reason for requiring an exemption must be included with the appeal request to facilitate further processing by the CSD.
* For cases falling under c): in case of against payment instructions, T2S already considers closing days for the relevant currency of the cash leg contained in an instruction to be settled in T2S (EUR and DKK calendars);
note in case of a cash leg settling outside T2S, it is the responsibility of the instructing party to use a settlement date aligned with the payment calendar.
* For cases falling under b) related to ISIN suspension from trading, it is important to note that CSDs do not have access to such information, which is managed at stock Exchange / trading venue level. CSDs would therefore reject the appeal of the participant, since the legitimacy of the exemption cannot be verified, unless ESMA FIRDS database identify those ISINs as “invalid for penalities”.

Regarding the handling of opening of insolvency proceedings against a participant, while an operational procedure exists in T2S, there is no specific functionality implemented in the T2S penalty mechanism to handle cash penalties stemming from an insolvency. Hence, CSDs would rely on existing T2S penalty mechanism functionalities and internal operational processes to ensure compliance with Article 7(2) and 7(12) of CSDR, as follows:

* Cash penalties should no longer be calculated in respect of settlement fails caused by the insolvent participant. The T2S insolvency framework ensures that no debit (cash or securities) new settlement instruction is submitted by the insolvent participant, however instructions already in the system and those credit new settlement instruction may still trigger cash penalties. These would need to be removed ex post by the CSD.
* Cash penalties calculated in respect of settlement instructions involving the insolvent participant until that date should be managed separately, i.e., not be included in the aggregated net amounts referred to in Article 17 of the RTS on Settlement Discipline. T2S provides a breakdown by participant, which enables the CSDs to segregate the amounts due / to be collected by the insolvent party).
* Cash penalties should not apply to settlement instructions relating to the liquidation of positions of an insolvent participant. In the case where such settlement instructions would be channelled via T2S and incur a cash penalty, it would need to be removed ex post by the CSD via current appeal process.

Finally, the two additional scenarios identified by ESMA as candidate for exemption of cash penalties are deemed relevant from an operational standpoint, i.e.:

* settlement instructions involving securities under sanctions or anti-money laundering proceedings;
* settlement instructions put on hold due to the order issued by a court, the police or similar authority with relevant mandate.

These scenarios can be handled with the existing T2S penalty mechanism functionalities, i.e., via the appeal process and ex-post removal of cash penalties. For this, new removal reasons are not deemed necessary.

<ESMA\_QUESTION\_SETD\_1>

1. ESMA would like to ask for the stakeholders’ views on the costs and benefits of the implementation of the respective exemptions from settlement discipline (based on the underlying causes of settlement fails that are considered as not attributable to the participants in the transactions). Please use the table below. Where relevant, additional tables, graphs and information may be included in order to support some of the arguments or calculations presented in the table below.

|  |  |
| --- | --- |
| **ESMA’s proposal - underlying causes of settlement fails that are considered as not attributable to the participants in the transactions** |    |
|   | **Qualitative description** | **Quantitative description/ Data** |
| **Benefits** |   |   |
| **Compliance costs:****- One-off****- On-going** |   |   |
| **Costs to other stakeholders** |   |   |
| **Indirect costs** |   |  |

<ESMA\_QUESTION\_SETD\_2>

Although all the cases put forward for exemptions from settlement discipline under Q1 can be handled with the existing T2S penalty mechanism functionalities and operational framework in place, implementing the corresponding operational procedures will have significant CSD costs which are to be considered, because ex-post activities would be necessary to be properly implemented and are also human resources consuming.

At this stage is not possible to provide accurate figures but we want to insist that costs will not be irrelevant including technical, functional and implementation costs, also considering the need of the adaptation of the corresponding penalties framework and procedures and the corresponding running costs.

<ESMA\_QUESTION\_SETD\_2>

1. Do you have other suggestions regarding the underlying causes of settlement fails that are considered as not attributable to the participants in the transactions? Please justify your answer and provide examples and data where available.

<ESMA\_QUESTION\_SETD\_3>

No other suggestion.

<ESMA\_QUESTION\_SETD\_3>

1. If you have answered yes to the previous question, please specify what costs and benefits you envisage related to the implementation of your proposal. Please use the table below. Where relevant, additional tables, graphs and information may be included in order to support some of the arguments or calculations presented in the table below.

|  |  |
| --- | --- |
| **Respondent’s proposal** (if applicable) |    |
|   | **Qualitative description** | **Quantitative description/ Data** |
| **Benefits** |   |   |
| **Compliance costs:****- One-off****- On-going** |   |   |
| **Costs to other stakeholders** |   |   |
| **Indirect costs** |   |  |

<ESMA\_QUESTION\_SETD\_4>

Not applicable

<ESMA\_QUESTION\_SETD\_4>

1. Do any of the exemption proposed above breaks the immunization principle? Please provide arguments.

<ESMA\_QUESTION\_SETD\_5>

We should consider several aspects on the so called (as it is not formal) immunization principle:

* Penalty procedures assign cash penalties at the level of CSD participant and transaction per transaction, without any consideration about the link of relationship among different transactions.
* On top of the previous statement, it is important to highlight that penalties have different calculation methodology depending of the transation type, as it can be seen:



Therefore, as it can be that the considered linked transactions the receipt is free of payment and the delivery is versus payment, etc., or not to be one receipt and one deliver, but several with several, or also to have different prices of the both transactions (or groups of them), we propose the so called ‘immunization principle’ is not as such and not to be considered.

 <ESMA\_QUESTION\_SETD\_5>

1. Which of the exemptions proposed above do you think can be filtered out before penalties are applied in an automated way? And which ones can only be exempted ex-post, as part of the already existing appeal mechanism at CSDs?

**Please provide details regarding the cost for ex-ante filtering compared to ex-post exemption via the appeal mechanism.**

<ESMA\_QUESTION\_SETD\_6>

Please consider answer to Q1 where each case is detailed with regard to ex-ante vs ex-post exemption.

At the moment the instances in the list are managed by CSDs and a process is in place as per ESMA Q&As and we do not see the benefits of changing the ways these scenarios are handled by the CSDs.

<ESMA\_QUESTION\_SETD\_6>

1. For exemptions that can be filtered out in advance, do you think that a CSD would prefer to implement this filter or not? Also considering the very large number of appeals they might have to deal with and also the costs it will entail.

<ESMA\_QUESTION\_SETD\_7>

As a general principle, there is a preference to manage exemptions in an automated manner (ex-ante filtering) since this reduces the operational workload of T2S CSDs and their communities. However, such ex-ante filtering is not always possible or relevant to implement e.g., to cover exceptional scenarios. In such case, the appeal process is to be seen the only solution/mitigation measure, although it would imply increasing the efforts and costs: we strongly support that the Ex-ante exemption must be the rule to avoid manual intervention needs across all stakeholders and appeals process must remain restricted to rare exception handling.

<ESMA\_QUESTION\_SETD\_7>

1. Do you agree with ESMA’s proposal regarding the circumstances in which operations are not considered as trading? Please specify which cases you agree with and which cases you don’t agree with (if applicable). Please justify your answer and provide examples and data where available.

<ESMA\_QUESTION\_SETD\_8>

The primary consideration is whether the type of operation proposed to be exempted: (i) can be identified unequivocally, and (ii) can be filtered ex-ante by the T2S penalty mechanism (i.e., built into the design), in order to be operationally manageable given the potential volumes of instructions to exempt.

Each settlement instruction in T2S must be filled in with a securities transaction type code[[1]](#footnote-1) also called ISO transaction code, to identify the type of transaction / operation it belongs to. However, the ISO transaction code field is not a matching criterion in the settlement instruction in T2S. Furthermore, the usage of certain ISO transaction codes is not harmonised, relying only on ISO description guidelines, which could lead to a high number of matching fails and degrade settlement efficiency if made as a matching criterion. Further harmonisation/market practices would be needed to reach a harmonised approach across CSDs and ultimately a T2S change request would need to be implemented to consider the field as a matching criterion, although a detail assessment must be done before having a decision on this not only on technical/functional aspects, but from an holistic point of view, mainly taking into account the undesirable collateral effects on settlement efficiency.

While CSDs can grant/restrict the usage of each ISO transaction code via privileges in T2S, most codes are made available to CSD participants when instructing to T2S.

With the above clarifications in mind, please find some considerations on each of the operation types put forward by ESMA as possible candidate for exemption:

* With regard to free-of-payment (FoP) securities transfers to securities accounts at CSDs in the context of the (de)mobilisation of collateral, such transfers belong to a wider range of collateral operations identified by several ISO transaction codes. Considering the usage of a specific code per type of collateral operation is not harmonised, embedding exemption in the T2S penalty mechanism based on the transaction type codes may lead to undesirable effects (e.g., wrong code used, both legs contain different codes, etc…).
* Regarding market claims and corporate actions on stock, the transaction type codes used in the settlement instruction are respectively ‘CLAI’ and ‘CORP’. An exemption for corporate actions on stock, based on the usage of the ‘CORP’ ISO transaction code (only granted to CSDs), is already in place in the T2S penalty mechanism. Based on the assumption that the usage of ‘CLAI’ is similarly restricted to CSDs, implementing an exemption for market claims in the T2S penalty mechanism based on the transaction type code is not a major technical adaptation and would possibly achieve the anticipated results.
* With regard to the process of technical creation of securities, meaning the transfer from the CSD’s issuance account to the issuer’s CSD account, the usage of the ISO transaction code ‘ISSU’ is not fully harmonised across CSDs and their participants. Unless the usage of the code is harmonised and properly controlled, an exemption is likely to provide undesirable effects. Furthermore, such technical transactions hardly fail when submitted to settlement.
* Concerning the creation and redemption of fund units on the primary market, meaning the technical creation and redemption of fund units (except for ETFs), the usage of the ISO transaction code ‘SUBS’ for subscription and ‘REDM’ for redemption is not fully standardised across CSDs and their participants. In addition, to identify the exact operation type and exclude ETFs, the asset type should also be considered. This would complexify the implementation of such exemption in the T2S penalty mechanism via ex ante filtering, and unless the usage of the code is harmonised and properly controlled, an exemption is likely to provide undesirable effects.
* Finally, concerning realignment operations, T2S realignment instructions are already filtered ex-ante from the scope of cash penalties, based on the transaction type code ‘REAL’ and the fact that they are T2S generated instructions. The rationale for this exemption is that in a T2S cross-CSD transaction, the delivering and receiving CSD participants can be identified, and the cash penalty does not need to be passed on through the chain of Issuer/Investor CSDs.

<ESMA\_QUESTION\_SETD\_8>

1. ESMA would like to ask for the stakeholders’ views on the costs and benefits of the implementation of the respective exemptions from settlement discipline (based on the circumstances in which operations are not considered as trading). Please use the table below. Where relevant, additional tables, graphs and information may be included in order to support some of the arguments or calculations presented in the table below.

|  |  |
| --- | --- |
| **ESMA’s proposal - circumstances in which operations are not considered as trading** |    |
|   | **Qualitative description** | **Quantitative description/ Data** |
| **Benefits** |   |   |
| **Compliance costs:****- One-off****- On-going** |   |   |
| **Costs to other stakeholders** |   |   |
| **Indirect costs** |   |  |

<ESMA\_QUESTION\_SETD\_9>

Based on the answer to Q8, one or several T2S change requests would be necessary to:

* Reach a wide consensus in the industry to setup the transaction code as mandatory matching field, to avoid inconsistencies between counterparties and
* Implement new exemptions embedded in the design of the T2S penalty mechanism (ex-ante filtering), with low/medium complexity, considering such filtering mechanism is already in place, including the corresponding testing to be performed to check that implementations are well done not only at CSD level but whole community.

In both cases, additional costs coming from this changes are to be considered to fully implements them on other areas than purely technical: documentation (legal functional, etc.) adaptations/changes, etc.

However, we would like to emphasize that in most cases the potential benefits should be carefully assessed considering the non-harmonised usage of the ISO transaction codes and potential non desirable collateral effects on settlement efficiency rates, which, high level assessment, cannot be underestimated.

<ESMA\_QUESTION\_SETD\_9>

1. Do you have other suggestions regarding circumstances in which operations are not considered as trading? Please justify your answer and provide examples and data where available.

<ESMA\_QUESTION\_SETD\_10>

No.

<ESMA\_QUESTION\_SETD\_10>

1. If you have answered yes to the previous question, please specify what costs and benefits you envisage related to the implementation of your proposal. Please use the table below. Where relevant, additional tables, graphs and information may be included in order to support some of the arguments or calculations presented in the table below.

|  |  |
| --- | --- |
| **Respondent’s proposal** (if applicable) |    |
|   | **Qualitative description** | **Quantitative description/ Data** |
| **Benefits** |   |   |
| **Compliance costs:****- One-off****- On-going** |   |   |
| **Costs to other stakeholders** |   |   |
| **Indirect costs** |   |  |

<ESMA\_QUESTION\_SETD\_11>

Not applicable

<ESMA\_QUESTION\_SETD\_11>

1. Do any of the exemption proposed above breaks the immunization principle? Please provide arguments.

<ESMA\_QUESTION\_SETD\_12>

Please see answer to Q5.

<ESMA\_QUESTION\_SETD\_12>

1. Which of the exemptions proposed above do you think can be filtered out before penalties are applied in an automated way? And which one can only be exempted ex-post, as part of the already existing appeal mechanism at CSDs?

Please provide details regarding the cost for ex-ante filtering compared to ex-post exemption via the appeal mechanism.

<ESMA\_QUESTION\_SETD\_13>

As a general principle, there is a preference to manage exemptions in an automated manner (ex-ante filtering) since this reduces the operational workload of T2S CSDs and their communities. However, an ex-ante filtering needs to be technically possible and leading to the desired outcome. Please refer to the answers to Q8 and Q9, i.e. only the case of market claims (ISO transaction code ‘CLAI’) could be beneficial based on the current usage of ISO transaction codes.

<ESMA\_QUESTION\_SETD\_13>

1. For exemptions that can be filtered out in advance, do you think that a CSD would prefer to implement this filter or not? Also considering the very large number of appeals they might have to deal with and also the costs it will entail.

<ESMA\_QUESTION\_SETD\_14>

Please refer to the answer to Q13.

<ESMA\_QUESTION\_SETD\_14>

1. Which transaction types based on the codes allowed by T2S (or potentially other codes such as ISO transaction codes) should be exempted from settlement discipline measures? Please provide the codes, their definition and arguments to justify the exemption.

<ESMA\_QUESTION\_SETD\_15>

Please see answer to Q13.

<ESMA\_QUESTION\_SETD\_15>

1. For example: a list of the 42 codes can be found in the T2S Scope defining documents, inter alia the [T2S User Handbook](https://www.ecb.europa.eu/paym/target/target-professional-use-documents-links/t2s/sdd/shared/pdf/T2S_UHB_R2024.JUN_clean_20240222.en.pdf), page 181 [↑](#footnote-ref-1)