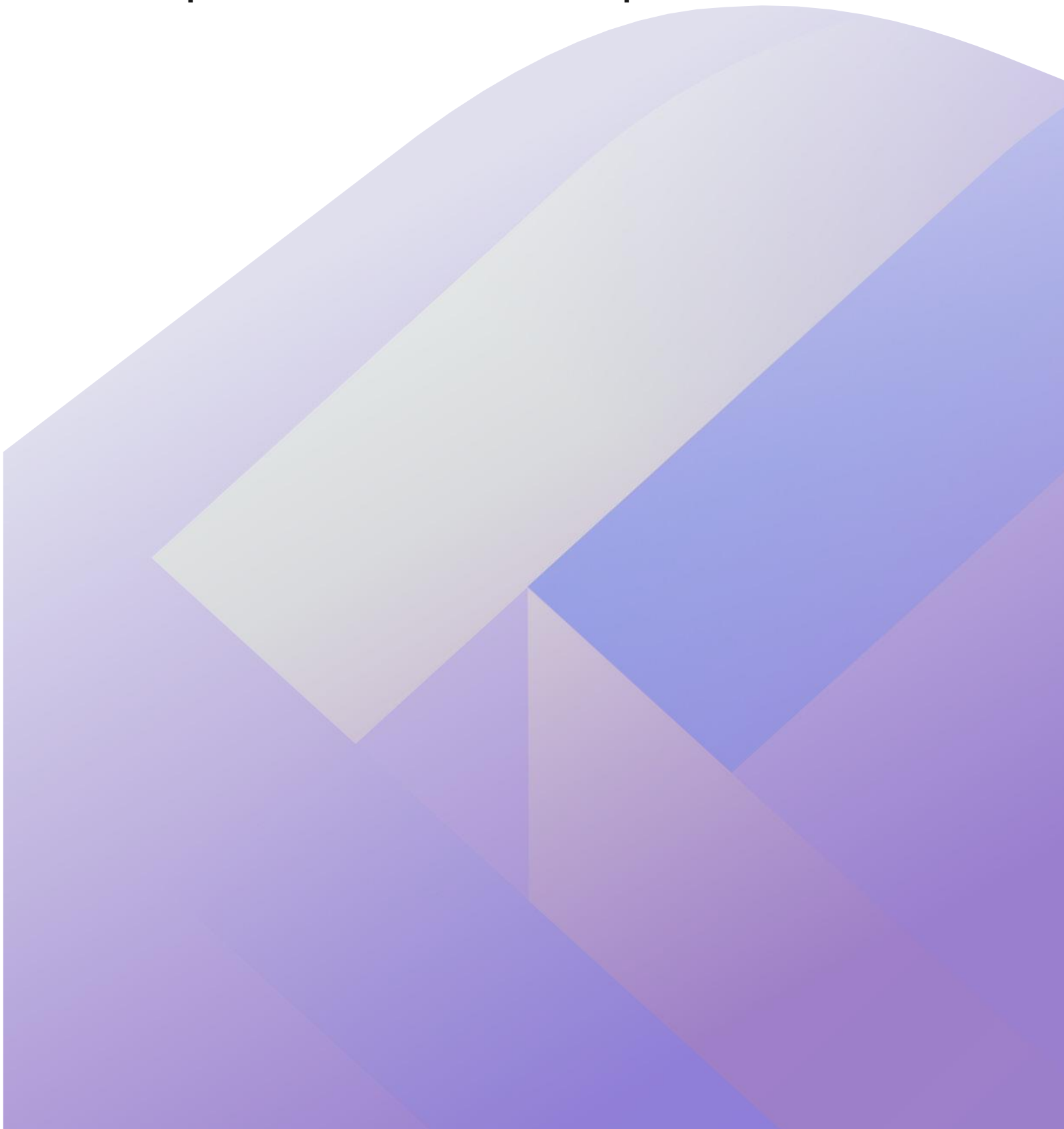


# Reply Form

**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](http://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](#)'.

## **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.

## 1 General information about respondent

Name of the company / organisation	European Central Bank / Market Infrastructure Board and CSD Steering Group
Activity	Other
Are you representing an association?	<input type="checkbox"/>
Country / Region	Europe

## 2 Introduction

The T2S Steering Level (i.e., Market Infrastructure Board and CSD Steering Group) welcomes the opportunity to respond to the consultation and provide the views from the T2S operator perspective. As such, all questions are answered considering the potential operational and functional impacts of ESMA's proposals on the T2S penalty mechanism. Policy aspects are not covered as part of the response.

## 3 Questions

**Q1 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>

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 T2S penalty mechanism 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](#) 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. Lacking such data, no exemption could be applied by CSDs or T2S penalty mechanism, and CSDs would reject the appeal of the participant, since the legitimacy of the exemption cannot be verified.
- 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 new settlement instruction is submitted by the insolvent participant, however instructions already in the system 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.<sup>1</sup>

<ESMA\_QUESTION\_SETD\_1>

**Q2 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.**

<b>ESMA's proposal - underlying causes of settlement fails that are considered as not</b>	
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<sup>1</sup> When using the code 'OTHR' an additional free text description is mandatory, which can help to cover a number of ad-hoc scenarios

attributable to the participants in the transactions		
	Qualitative description	Quantitative description/ Data
<b>Benefits</b>		
<b>Compliance costs:</b> - One-off - On-going		
<b>Costs to other stakeholders</b>		
<b>Indirect costs</b>		

<ESMA\_QUESTION\_SETD\_2>

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, except for cases related to an ISIN suspended from trading as CSDs do not have access to information maintained at stock exchange / trading venue level and cannot verify the legitimacy of the exemption. Under the assumptions taken in the reply to Q1, no implementation costs on T2S operator side are anticipated.

<ESMA\_QUESTION\_SETD\_2>

**Q3 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>

**Q4 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
<b>Benefits</b>		
<b>Compliance costs:</b> - One-off - On-going		
<b>Costs to other stakeholders</b>		
<b>Indirect costs</b>		

<ESMA\_QUESTION\_SETD\_4>

Not applicable.

<ESMA\_QUESTION\_SETD\_4>

**Q5 Do any of the exemption proposed above breaks the immunization principle? Please provide arguments.**

<ESMA\_QUESTION\_SETD\_5>

The immunisation principle goes beyond the operational aspects of T2S penalty mechanism since T2S only assigns cash penalties at the level of CSD participant and not further down the chain of intermediaries.

<ESMA\_QUESTION\_SETD\_5>

**Q6 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.

<ESMA\_QUESTION\_SETD\_6>

**Q7 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 feasible or relevant to implement e.g., to cover exceptional scenarios. In such case, the appeal process is deemed suitable. Please consider answer to Q1, i.e., the proposed list of exemptions is deemed operationally manageable with the current set of T2S penalty mechanism functionalities and operational framework in place, except for the ISIN suspension from trading, as also mentioned in Q2.

<ESMA\_QUESTION\_SETD\_7>

**Q8 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>

From the T2S operator perspective, 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<sup>2</sup> also called ISO transaction code, to identify the type of transaction / operation it belongs to.

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<sup>2</sup> A list of the 42 codes can be found in the T2S Scope defining documents, inter alia the [T2S User Handbook](#), page 181

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 market practices would need to be put in place to reach a harmonised approach across CSDs and ultimately a T2S change request would also need to be implemented if considering the field as a matching criterion.

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 would probably lead to inconsistent results regarding the application of the exemption due to e.g., different codes used for a certain transaction type, both legs of the transaction containing 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 allow to achieve the anticipated results, i.e., a consistent application of the exemption.
- 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 inconsistent results. Furthermore, such technical transactions rarely 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 inconsistent results.

- 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>

**Q9 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.**

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

<ESMA\_QUESTION\_SETD\_9>

Based on the answer to Q8, one or several T2S change requests would be necessary to 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. However, in most cases the potential benefits should be carefully assessed considering the non-harmonised usage of the ISO transaction codes. The implementation of an exemption related to creation and redemption of fund units on the primary market would be more complex since it requires to identify the asset type in addition to the ISO transaction code in the T2S penalty mechanism.

<ESMA\_QUESTION\_SETD\_9>

**Q10 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>

This is a policy consideration not covered by the T2S operator reply.

<ESMA\_QUESTION\_SETD\_10>

**Q11 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.**

<b>Respondent's proposal (if applicable)</b>		
	<b>Qualitative description</b>	<b>Quantitative description/ Data</b>
<b>Benefits</b>		
<b>Compliance costs:</b> - One-off - On-going		
<b>Costs to other stakeholders</b>		
<b>Indirect costs</b>		

<ESMA\_QUESTION\_SETD\_11>

Not applicable.

<ESMA\_QUESTION\_SETD\_11>

**Q12 Do any of the exemption proposed above breaks the immunization principle? Please provide arguments.**

<ESMA\_QUESTION\_SETD\_12>

The immunisation principle goes beyond the operational aspects of T2S penalty mechanism since T2S only assigns cash penalties at the level of CSD participant and not further down the chain of intermediaries.

<ESMA\_QUESTION\_SETD\_12>

**Q13 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, i.e., a consistent application of exemptions. Please refer to the answers to Q8 and Q9: beyond the exemptions already in place for CA on stock and T2S realignments, only the case of market claims (ISO transaction code 'CLAI') has been identified as potential candidate for exemption based on the current usage of ISO transaction codes.

<ESMA\_QUESTION\_SETD\_13>

**Q14 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>

**Q15 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>

This is a policy consideration not covered by the T2S operator reply.

<ESMA\_QUESTION\_SETD\_15>