

# SURVEY ON TOPICS FOR THE CSDR REVIEW

Fields marked with \* are mandatory.

## SURVEY ON TOPICS FOR THE CSDR REVIEW

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### Background

Following a request from the European Commission, in light of the upcoming review of Regulation (EU) No 909/2014 (CSDR)[1], ESMA would like to gather input from CSD competent authorities[2] (NCAs) and relevant authorities[3] (RAs), EBA, and Trade Associations regarding possible suggestions for amending C S D R .

[1] Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014R0909>)

[2] As defined in Article 11(1) of CSDR.

[3] As defined in Article 12(1) of CSDR.

### Process

NCAs, RAs, EBA, as well as ECSDA, EACH, AFME, EBF, ICMA, EuropeanIssuers, ISLA, FIA, and EFAMA will be asked to fill in the survey included below by **10 July 2020**.

ESMA staff will share the answers with the European Commission and with the ESMA Post Trading Standing Committee (PTSC).

### Instructions

Answers should be submitted by **10 July 2020**.

In case you have any questions or you encounter technical problems, you can contact Alina Dragomir (Alina.Dragomir@esma.europa.eu) and Karole-Anne Sauvet-Frot (Karole-Anne.Sauvet-Frot@esma.europa.eu).

## Survey on Topics for the CSDR Review

### General information

\* 1 Choose your jurisdiction:

*at most 1 choice(s)*

EU

\* 2 Please, provide the name of your institution/ organisation:

International Securities Lending Association

\* 3 Capacity:

*at most 1 choice(s)*

- Competent Authority
- Relevant Authority
- EBA
- Trade Association

5 Please provide the names of the members which have contributed to your answers:

<https://www.isla.co.uk/our-members/>

6

If applicable, please, provide the name of the CSD(s) for which you are Competent Authority/ Relevant Authority:

Please, provide the contact details of the person answering this questionnaire:

\* 7 Name:

Farrah Mahmood

8 Position:

\* 9 Email:

farrah.mahmood@isla.co.uk

## Survey

\* 1 Do you consider the CSDR requirements could be improved or further clarified?

*at most 1 choice(s)*

- Yes
- No
- No opinion

2 If yes, please provide suggestions for potential amendments to the existing CSDR requirements. Please fill-in the relevant row for each article for which you are proposing amendments:

[1] Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014R0909>)

	Regulation (EU) No 909/2014 (CSDR)[1] – current provisions	Suggested amendments	Justification including evidence and data
Article 1			
Article 2			
Article 3			
Article 4			
Article 5			
Article 6			
		<p>ISLA and its members propose that Article 7(3) CSDR should be replaced with a provision directing ESMA, in close cooperation with the members of the ESCB, to undertake a market impact assessment of a potential regulatory buy-in process as outlined further below. The assessment should include recommendations for the possible design of such a process, considering different markets, instruments, and transaction types, as well as the likely impacts on the smooth and orderly functioning of the markets concerned. As such, Articles 21-38 of the RTS would not take effect until this review has been completed.</p> <p>More specifically, ISLA proposes that:</p> <p>A) The penalties framework should be introduced as outlined in the RTS, but the mandatory buy-in requirements should not.</p>	

P (3) Without prejudice to the penalty mechanism referred to in paragraph 2 and the right to bilaterally cancel the transaction, where a failing participant does not deliver the financial instruments referred to in Article 5(1) to the receiving participant within 4 business days after the intended settlement date ('extension period') a buy-in process shall be initiated whereby those instruments shall be available for settlement and delivered to the receiving participant within an appropriate time-frame. Where the transaction relates to a financial instrument traded on an SME growth market the extension period shall be 15 days unless the SME growth market decides to apply a shorter period.

P (4 )The following exemptions from the requirement referred to in paragraph 3 shall apply:

(a) based on asset type and liquidity of the financial instruments concerned, the extension period may be increased from four business days up to a maximum of seven business days where a shorter extension period would affect

Instead, any introduction of regulatory buy-in requirements should be delayed until regulators have had the opportunity to perform an in-depth review, to assess the extent to which the penalties framework has improved overall settlement discipline, over a 2-year period.

B) After this period, ESMA should conduct a thorough impact assessment of the penalties framework and adjust the penalties accordingly per asset class, dependent on the improvement of settlement efficiency.

C) After a further period, ESMA should conduct an impact assessment on the penalty structure and, where specific asset classes have not shown significant improvement in settlement efficiency, may consider introducing a buy-in mechanism. However, any such buy-in mechanism should be introduced only once the issues outlined in the justification section have been addressed and following a further public consultation.

We note that if these requested amendments are made, then the current provisions of paragraphs 4, 6, 7 and 15 relating to mandatory buy-ins will also become obsolete. However, our suggested amendments to these paragraphs set out below would be relevant to the extent that a regulatory buy-in requirement is retained or reintroduced following the further review envisaged here.

ISLA and its members are proposing that the provisions of Article 7 CSDR that impose mandatory buy-in requirements should be deleted from the level 1 text. This would allow the introduction of regulatory buy-in requirements to be postponed until a complete review and impact assessment can be undertaken and necessary amendments made to the buy-in requirements currently set out in Article 7 CSDR.

Those amendments are outlined in the joint associations letter to the European Commission and ESMA dated 22nd January 2020, of which ISLA was a signatory - [https://www.isla.co.uk/wpcontent/uploads/2019/03/Joint\\_Associations\\_Letter\\_EC\\_ESMA\\_CSDR.pdf](https://www.isla.co.uk/wpcontent/uploads/2019/03/Joint_Associations_Letter_EC_ESMA_CSDR.pdf).

In summary, the issues requiring review and revision prior to implementation are as follows:  
i. Symmetrical payments obligations –

Article 7

the smooth and orderly functioning of the financial markets concerned;

(b) for operations composed of several transactions including securities repurchase or lending agreements, the buy-in process referred to in paragraph 3 shall not apply where the time-frame of those operations is sufficiently short and renders the buy-in process ineffective.

P (6) Without prejudice to the penalty mechanism referred to in paragraph 2, where the price of the shares agreed at the time of the trade is higher than the price paid for the execution of the buy-in, the corresponding difference shall be paid to the receiving participant by the failing participant no later than on the second business day after the financial instruments have been delivered following the buy-in.

P(7) If the buy-in fails or is not possible, the receiving participant can choose to be paid cash compensation or to defer the execution of the buy-in to an appropriate later date ('deferral period'). If the relevant financial instruments are not delivered to the receiving participant at the end of the deferral period, cash compensation shall be paid. Cash compensation shall be paid to the receiving participant no later than on the second business day after the end of either the buy-in process referred to in paragraph 3 or the deferral period, where the deferral period was chosen.

P (15) ESMA shall, in close cooperation with the members of the ESCB, develop draft regulatory technical standards to

A suggested amendment to Paragraph 4 would be to expressly exclude the following from the mandatory buy-in requirements:

- (a) all Securities financing transactions - as per questions raised on ESMA's new Q&A tool q23 - awaiting guidance from the Commission
- (b) collateral movements
- (c) intra-entity transfers of securities;
- (d) other transactions that do not directly represent the transfer of ownership of a security.

A suggested amendment to Paragraph 6 (and multiple other paragraphs in Article 7) would be to include more clarity on the definition of 'participant' which is not used consistently throughout the text. After a comprehensive review, the terms used should ensure that it is clear who is the correct party to act in the relevant situation. In the context of securities lending transactions (where trading parties are generally expected to be responsible for executing buy-ins as envisaged under the RTS) ISLA would propose reflecting this in the Level 1 text also, by replacing the term 'participant' with 'trading party', where relevant.

ISLA also consider it is important that the price difference can be settled symmetrically between the parties with respect to a buy-in or in the case of cash compensation. Article 7(6) CSDR as currently drafted provides for the payment of the price difference to be paid in the wrong direction. This error was partially corrected via the RTS (where the price difference is 'deemed

suggested amendment to Art 7(6)

- ii. The possibility for a pass-on mechanism – suggested provision to be included to Art 7(8)
- iii. Clearer definition of scope – suggested amendment to Art 7(4) (as per feedback from a joint ISLA and ICMA survey regarding the treatment of open SFTs, submitted to ESMA in February 2020).
- iv. Appropriate extension periods – suggested amendment to Art 7(7)
- v. Suitability of a cash settlement mechanism – suggested amendment to Art 7(7)
- vi. Discretionary appointment of buy-in agent / consequence of not being able to appoint a buy-in agent.

ISLA are also yet to receive guidance on a number of open Q&A's relating to these issues - <https://www.esma.europa.eu/press-news/esma-news/esma-starts-publishing-questions-received-through-its-qa-process>. It is crucial that the market has clarity on these scoping and interpretational issues well in advance of the application of any regulatory buy-in requirements, as they will have a significant impact on contractual and systems changes that firms will need to make in order to implement such requirements effectively.

More generally, ISLA supports the adoption of the penalty regime as laid out in Article 6 CSDR – 'Measures to prevent settlement fails'. However, ISLA members agree that the adoption of the mandatory buy-in regime as it

specify: (c) the details of operation of the appropriate buy-in process referred to in paragraphs 3 to 8, including appropriate time-frames to deliver the financial instrument following the buy-in process referred to in paragraph 3. Such time-frames shall be calibrated taking into account the asset type and liquidity of the financial instruments;

(d) the circumstances under which the extension period could be prolonged according to asset type and liquidity of the financial instruments, in accordance with the conditions referred to in point (a) of paragraph 4 taking into account the criteria for assessing liquidity under point (17) of Article 2(1) of Regulation (EU) No 600 /2014;

(e) type of operations and their specific time-frames referred to in point (b) of paragraph 4 that renders buy-in ineffective;

(f) a methodology for the calculation of the cash compensation referred to in paragraph 7; frames referred to in point (b) of paragraph 4 that renders buy-in ineffective;

(f) a methodology for the calculation of the cash compensation referred to in paragraph 7;

paid' in the circumstances described in Article 7 (6) CSDR). Article 7(6) also refers to 'shares' rather than 'securities. Therefore, if the buy-in provisions of CSDR are retained, ISLA proposes fully correcting these points and providing for symmetric payments with respect to the price difference, as follows:

- (i) Where the value of the securities agreed at the time of the trade is lower than the value of the buy-in, the corresponding difference shall be paid by the failing trading party to the receiving trading party.
- (ii) Where the value of the securities agreed at the time of the trade is higher than the value of the buy-in, the corresponding difference shall be paid by the receiving trading party to the failing trading party.

A suggested amendment to Paragraph 7: ISLA feels that specific extension periods should not be prescribed in the Level 1 text. Extension periods should be based on factors such as market structure, liquidity and market conditions and should be determined only after an extensive review by ESMA and/or public consultation, prior to implementation of any buy-in regime. Further, if it is not viable to calculate an appropriate value for cash settlement, the receiving party should be able to choose to defer the buy-in indefinitely, until it is possible to do so.

Article 25 of the RTS as mentioned in Article 7 (15), requires CCPs, clearing members, trading

stands under Article 7 CSDR would in fact negatively impact the efficiency of European capital markets and thus would not be in line with the wider objectives of the Capital Markets Union, leading to greater costs and barriers to investing in European securities. As such, ISLA and its members feel that a phased in approach to address settlement discipline, would be more effective at decreasing settlement fails across the industry.

Further, securities lending, in itself, is a mechanism used to avoid or reduce the likelihood of settlement fails occurring on cash transactions. However, the CSDR mandatory buy-in regime as it stands is not well tailored to the structure and dynamics of securities lending transactions. Hence, imposing mandatory buy-ins in relation to securities lending transactions (as the rules currently stand) could be counterproductive as it may disincentivise securities lending in Europe altogether.

		venue members, and trading parties to have procedures in place to execute the buy-in process, and to establish contractual arrangements with their clients to ensure that the buy-in requirements are enforceable in all jurisdictions. Work is already being undertaken by ISLA to comply with the requirements of Article 25 and contractual provisions will need to be agreed with counterparts to reflect the mandatory buy-in requirements. However, the global reach of these requirements, extending to all trading parties undertaking securities lending transactions in in-scope financial instruments will require a global re-papering exercise. This will be a complex exercise and a huge cost to the industry. This is therefore another reason why ISLA supports a postponement of the mandatory buy-in requirements of Article 7 CSDR until a thorough review and impact assessment has been completed.	
Article 8			
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## Contact

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