

Règlement CSD Impacts pour la Place Française

GLF

Version intermédiaire

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1 Introduction

1.1 Purpose of the document

Regulation (EU) No. 909/2014 of the Parliament and of the Council on improving securities settlement in the European Union and on central securities depositories, or CSDR, has come into effect on September 17, 2014.

If some of its provisions are already applied, such as settlement on T+2, most will only be effective from 2019 or later, in connection with the authorisation of European Central Securities Depositories under CSDR, and the enforcement of settlement provisions.

This document is an **interim version of the specifications** listing and explaining the impacts of these provisions for the French financial institutions.

The following inputs are expected to finalise the specifications:

- The replies to the questions asked to ESMA by the T2S CSDR Task Force, under the umbrella of the ECB,
- The publication of the final version of the ECSDA Settlement Fails Penalties framework,
- The work undertaken by european professional associations on buy-ins, pending some clarification from the regulator,
- The publication of the ESMA guidelines related to allocations/confirmations.

Topic		Coverage in this version
CSD / ICSD authorisation		Covered
Internalised Settlement		Covered
Settlement Discipline	Confirmations / Allocations	Partially covered
	Penalties	Partially covered
	Buy-ins	Will be covered in a later version in coordination with AFME's work.

1.2 CSD Regulation: background

The main objectives of this regulation are to increase the safety and efficiency of securities settlement, and to define an harmonised prudential framework to oversee the activities of central securities depositories ("CSD").

The CSD regulation originates from three main sources:

- Provide a regulatory response to some barriers identified in the Giovannini reports of 2001 and 2002, including:

- Differences in the processing practices of settlement processes, including differences in the settlement cycle duration,
- Some differences in the processing of corporate actions, and in the holding and custody rules,
- Settlement not irrevocable during the day cycle,
- National differences in securities issuance practices,
- National restrictions on securities location.
- Continue to harmonise the regulatory framework applicable to market infrastructures, in particular after strengthening the rules governing the financial markets and the clearing houses (MIFID I & II, EMIR), and determine common rules for CSD activities, most of which are now competing at European level with the implementation of Target2-Securities (T2S).
- Provide a regulatory framework for the implementation of T2S.

The CSD regulation modifies and extends the "Settlement Finality Directive" (SFD), which dealt exclusively with settlement and left some flexibility to local regulators and governments to define and oversee the settlement systems. But it goes further, since the regulation covers all activities of central depositories, including the centralised maintenance of accounts and the notary function, and establishes the rules within a European legal framework.

The harmonisation objective covered by the CSD regulation can be divided into 4 major categories:

- Standardisation of central depositories authorisation processes (including the definition of activities that can be managed by central depositories, as well as the segregation from banking activities),
- Standardisation of the prudential framework,
- Standardisation of the rules governing the provision of settlement services,
- Standardisation of the rules governing the provision of centralised account maintenance services and notary services.

The regulatory framework, consisting of the regulation and the delegated acts established on the proposal of ESMA and EBA on CSDR, must be implemented, to date, based on the following schedule:

	2014	2015	2016	2017	2018	2019	2020						
CSD Regulation	★ Entry into force of CSD Regulation (09/2014)												
Delegated Acts	<div style="border: 1px solid gray; padding: 5px; width: fit-content;"> ESMA / EBA Open public consultation + ESMA Final Reports submitted to the European Commission </div>												
CSD Requirements & Prudential framework / Banking-type ancillary services								Publication of « RTS » and « ITS » in the official journal of the EU (03/2017) ★		★ Publication of « RTS » in the official journal of the EU (11/2016)		★ Entry into force of requirements for CSDs / ICSDs upon their authorisation (mid 2018)	
Internalised settlement								★ Publication of « RTS » and « ITS » in the official journal of the EU (03/2017)		★ Entry into force of Internalised settlement requirements (03/2019)			
Settlement discipline								★ Publication of « RTS » in the official journal of the EU (09/2018)				★ Entry into force of settlement discipline requirements (09/2020)	
Impacts for French financial institutions				★ CSD / ICSD authorisation (From Q2 2018)	★ Internalised Settlement requirements implementation (1 st reporting in July for april-june period)	★ Settlement discipline requirements implementation (13/09/2020)							

1.3 Study scope

Instruments & transaction types

The provisions of the CSD regulation impact all financial instruments issued, settled and held in custody through a central securities depository within the European Union:

- whether or not these instruments are admitted to trading or traded on a trading venue;
- whether or not they are cleared by a central counterparty;
- whether they are the subject of a definitive disposal (purchase, sale) or a temporary disposal (repo, lending/borrowing of securities);
- whether or not it is an instruction at the initiative of a counterparty → *the processing of automatically generated instructions is presented in each chapter.*

Hence, this impact assessment is focused on all types of potentially impacted instruments:

Shares and equivalent	Warrants
Units in collective investment undertakings (UCITS, AIF or others)	Emission allowances
Sovereign and private bonds, including exchangeable debt securities	

It should be noted that *American Depositary Receipts (ADR)* and *Global Depositary Receipts (GDR)*, being issued on the American market, are excluded from the scope.

Stakeholders

This assessment focuses on the impacts for French financial institutions, affiliates of Euroclear France or of International CSD (ICSD). It covers in particular the impacts for institutions with the following status:

- Banks dealing on own account;
- Broker-dealers and clearers;
- Custody account-keeper;
- Issuers and their agents;
- Depository banks of collective investment undertakings;
- Where applicable, asset managers and other institutional investors.

However, it does not cover the impacts on market infrastructures, namely the central securities depositories, clearing houses and trading venues.

Process

The proposed assessment covers the following processes:

- Issuance-related processes, including the initial recording of the instrument and related tasks (e.g. obtaining a LEI);
- Settlement;
- Custody-related processes, including processing of corporate actions and coupons/redemption.

However, it should be noted that only the processes involving the following central securities depositories are covered:

- Euroclear France, which remains the main analysis approach;
- Euroclear Bank;
- Clearstream Banking Luxembourg.

Except in particular cases, processes involving other central depositories of the EU or central depositories outside EU recognised by ESMA will not be addressed by this impact assessment.

1.4 Challenges

5 major investigation topics have been identified, each topic with specific challenges for the market:

- **Impacts of the CSD & ICSD authorisation:** the challenge on this topic, to be confirmed by the CSD/ICSD as part of their authorisation procedure under CSDR, is as follows:
 - Anticipate possible evolutions in terms of relationship between CSD/ICSD and their affiliates;
 - Ensure a smooth transition in terms of process and service delivery if the authorisation obtained requires changing the scope of some services or their conditions of exercise or membership – in particular for ICSDs, as part of the implementation of the "banking-type ancillary services" provided by CSDs, which will continue to be provided through a 'limited purpose bank'.
 - Anticipate possible evolutions related to specific regulatory requirements impacting CSDs (integrity of issue and related reconciliations, account structure imposed by the regulation).
 - Offer to their clients the choice between the use of segregated accounts or the use of an omnibus account in the CSD books (mandatory for a CSD authorised under CSDR)
- **Confirmations/Allocations:**

Define the adaptations to be made on market practices in order to facilitate the processing of confirmations and affirmations within the time limits imposed by ESMA.

Note: See also the impacts on settlement
- **Penalty scheme:**
 - Define practices to limit the triggering of penalties, a new measure designed to prevent settlement defaults.
 - Adapt to the future harmonized penalty scheme applicable to all EU CSDs (set up in countries where there are currently none, replacing it for others).
 - Analyse settlement cases between two CSDs which do not use the same penalty scheme, or with a CSD from a third country (in particular the UK) and if necessary, define local practices.

- **Buy-in processing:** define, within the framework imposed by the regulation, market procedures and practices for the smooth processing of buy-in procedures, irrespective of the type of instrument.
- **Internalised settlement:** harmonise the understanding of regulatory requirements at the market level and identify impacts for custodians and their clients.

2 Impact summary

The main impacts of the analysis conducted at this stage of the regulatory publications and on the scope covered by this version are as follows, by type of stakeholder:

	All participants	Specific case
Impacts of the CSD & ICSD license		
Major impacts	No major impact identified, apart from CSD being authorized on different dates, with subsequent impacts for participants starting on said different dates	Custodians: Definition of a policy of asset segregation (account-keepers are required to propose to their clients the choice between the use of segregated accounts or the use of an omnibus account in the CSD books)
Internalised settlement		
Major impacts	<p>The legal entity which is the legal custodian of the accounts where the internalized settlement takes place has the obligation to report</p> <p>A legal entity will send its internalized settlement reporting to its National Competent Authority</p> <ul style="list-style-type: none"> • All internalized settlements done by the legal entity must be reported in a single report • The legal entity can delegate to a third-party the submission of the reporting to the NCA • The communication protocole remains to be confirmed for each NCA <p>The AFTI is working with the French Regulator to define a test planning for Q2 2019</p> <ul style="list-style-type: none"> • The number of reportings and the number of senders currently under assessment <p>No issue identified regarding the calculation of the different totals to report</p>	-

	<p>Net settlements corresponding to the netting or the aggregation of several buys or sells executed on a market are not in the scope of the internalized settlement reporting since the unitary settlement instructions are not internalized settlements.</p>	
Confirmations/Allocations		
Major impacts	<p>No major impact identified, to be confirmed with the results of the ESMA consultation ESMA70-151-2040</p> <p>Main points highlighted during the analysis</p> <ul style="list-style-type: none"> • Transaction type mandatory • Usage of electronic channels recommended • Generalisation of the usage of SSI advised 	-
Settlement discipline: Settlement fails penalty scheme		
Major impacts	<p>Usage of T2S calculation engine for fails penalties for T2S CSD; fails penalties for non T2S flows will be calculated via other calculation engines</p> <p>Custodians should have the capacity to calculate penalties to ensure correct allocation and sufficient transparency to their clients</p> <ul style="list-style-type: none"> • When penalties are charged by CSD on net/aggregated settlement instructions, the custodian should be able to allocate per final client the related penalties • Penalties should also apply to internalized settlements • Provide details upon client dispute <p>Brokers and Asset managers have an essential role in fails prevention and penalties reduction</p> <ul style="list-style-type: none"> • Brokers by monitoring more closely the transactions, by being able to prioritise the instructions to settle and by sourcing reliable SSI from their clients • Asset managers by providing detailed SSI to their agents and by optimising the usage of the affirmation-confirmation process <p>No golden source available for reference data (prices, CFI codes, Most Relevant Market, etc.)</p> <ul style="list-style-type: none"> • All entities calculating penalties will have to source these data 	-

	<ul style="list-style-type: none">• Penalties may differ depending on the entity calculating the penalties, or for cross-border transactions <p>Principle to avoid multiple penalties to be charged on the same fails still to be confirmed by CSDs</p>	
Settlement discipline : Mandatory buy-in procedures → not covered in this version		

3 Guiding principles and dependencies

3.1 Other regulatory changes and market projects in France

As to comply with CSDR, Chapter V of the AMF's general regulation has been modified by decree on 23rd October 2018 and published in the Official Journal on 28th October 2018. The modifications consist in:

1. The creation of a Chapter VI bis applicable to Central Depositories authorised under CSDR. Central Depositories not yet authorised under CSDR must comply with Chapter V and VI
2. The adaptation of Chapter VII related to the transfer of ownership of financial instruments
3. The removal or adaptation of the clauses addressed by the CSDR regulation or by the Monetary and Financial Code. Amongst these adaptations, the obligation to record the entirety of an issue when admitted to a CSD is removed for all types of financial instruments.

3.2 Other regulatory changes and market projects at European level

This impact assessment is especially based on the results of the work carried out under the following projects:

- Work of the Penalties Task Force, initiated under the umbrella of the ECB in 2016 in order to draft specifications for the development of a penalty calculation module in T2S
- Work carried out by the ECSDA concerning the drafting of a Framework of harmonised practices for the management of penalties for the central securities depositories.
- Work carried out by the "Association for Financial Markets in Europe" (AFME), by the "International Capital Market Association" (ICMA) and by the "European Banking Federation" (EBF), regarding the CSD regulation, in particular the topic of internalised settlement, as well as buy-in processing and currency processing in case of penalties.

4 Impact assessment

4.1 Impacts of the CSD & ICSD authorisation

The list of CSD authorised under CSDR is available on the ESMA website :

https://www.esma.europa.eu/sites/default/files/library/esma70-151-889_csd_register.pdf

4.1.1 Euroclear (CSDs ESES, Euroclear Bank)

4.1.1.1 *Evolution in the relationship with participants*

i. Membership conditions and price transparency

Euroclear ESES and Euroclear Bank have brought changes to their 'Terms & Conditions' and other legal documentation.

There is no significant change to be expected in the account opening procedure under CSDR, both on ESES and Euroclear Bank side, except that participants will need to have a valid LEI and to share its renewals with Euroclear. The account opening forms have been adapted to collect these additional information: The LEI and the account type (see Point d.).

Note that in the account opening procedure, participants are asked about the account structure they wish to adopt.

ii. Governance

ESES has user committees in place in Belgium, France and the Netherlands, in the form of 'Market Advisory Committees (MACs)'. The 'Terms of Reference (ToRs)' and the composition of MACs have been adapted to comply with CSDR principles on user committees, and have become the "Users Committees". The first 'official' user committee was held in September 2017. The selection criteria are public and available in the 'ToRs' on the Euroclear site. The goal is to have a wide range of participants from all market segments.

A user committee in accordance with CSDR principles was set up in Euroclear Bank in September 2017.

4.1.1.2 *Conditions of security recording*

Regarding "passporting", ESES and Euroclear Bank will request passports enabling them to act as 'issuer CSD', at least on the foreign values for which they already act as issuer CSD. When CSDR is fully in place, Euroclear will only be allowed to accept securities for which the competent authorities have given their authorisation. As stated in ESMA's Q&A, ESES and Euroclear Bank will not be allowed to accept securities whose issuer's LEI would not have been provided. It must be a valid LEI based on the details provided by ESMA.

4.1.1.3 *Integrity of issue & Reconciliations*

ESES and Euroclear Bank will block the security settlement, if the creation or disappearance of securities would not be resolved in T+1 (reconciliation problem).

Daily reconciliations must be carried out by the institutions with the EU's central securities depositories to which they are affiliated. Particular attention must be paid to reconciliations concerning units in

collective investment undertakings, for which reconciliations are currently sometimes carried out less frequently.

4.1.1.4 *Asset segregation*

See in *f. Record-Keeping*

It should be noted that participants will also have to offer asset segregation to their clients. Participants must offer to their clients at least the choice between a segregation by omnibus client account or by individual client account. They must also inform them of the costs and risks associated with each option, like CSDs must inform their participants.

4.1.1.5 *Banking services*

Euroclear Bank will have a specific and limited banking license, allowing it to provide only the following services:

- Banking Services in connection with settlement: cash accounts, overnight credit facilities, cash lending for pre-financing or securities lending.
- Payment Services
- Grant of guarantees and subscription of commitments related to securities lending/borrowing
- Cash flow activities involving the foreign exchange markets and the securities related to the participants' credit balance management.

Euroclear Bank will ensure that all credit facilities are collateralised (except for entities exempted by CSDR).

4.1.1.6 *Record-Keeping*

ESES

The ESES CSDs have sent a newsletter to their clients, dated 25/1/2017 (2017-NL-003), specifying the impacts of CSDR regarding Record Keeping requirements on their **account structure**. Clients are asked to check the information held by Euroclear (legal entity, type of asset, cash account...) and to complete them with the new data required by CSDR:

- the LEI (Legal Entity Identifier) of their legal entity (see point a.i.),
- the profile of their legal entity (CSD or non-CSD),
- the country of registration of their legal entity,
- the country of residence of their legal entity,
- the type of their legal entity: parent company, branch or subsidiary

Under CSDR, assets are categorized into 3 types the ESES CSDs had to adopt. As holding type 00 (undifferentiated assets) is no longer admitted under CSDR, ESES clients had to choose between the 3 types allowed under CSDR. To do so, the ESES CSDs have created 2 new types of holding:

- type 10: 'individual client assets'
- type 11: 'assets held on behalf of a CSD'

CSDR requires CSDs to **identify the 'Payment banks'** used for the settlement of instructions and to store this information. ESES clients must report to CSDs, for each cash account (DCA) they use:

- the legal name of their 'Payment bank',
- the LEI of their 'payment bank',
- the country of registration of their 'payment bank',
- the country of residence of their 'payment bank'

As part of CSDR, the ESES CSDs also had to adapt the **securities application form**, see the newsletters of 18/4/2017 and 1/6/2017 (2017-NL-017). This form must now contain 2 additional fields:

- The 'Governing Law': The 'Governing Law' governs the 'terms & conditions' of an issue. In this field, clients must indicate the 2-digit ISO 3166 code, which identifies the country of the issue's Governing Law,
- The LEI of the issuer (see point b.)

Euroclear also adapted its Plug & Clear tool to add the 'Governing law' (newsletter 2017-NL-015 of 28/3/2017).

Euroclear Bank

Euroclear Bank has sent to its clients a newsletter dated 17/11/2016 (2016-N-060), specifying the impacts of CSDR regarding Record Keeping requirements on their **account structure**. Clients had to check the information held by Euroclear, and complete it in case of any missing data:

- the profile (CSD or non-CSD) of their institution,
- the LEI (Legal Entity Identifier) of their institution (see point a.i.),
- the country of registration of their institution,
- the registration number of their institution,
- the account number
- the account name
- the account type (own account (OW), individual client account (IS), omnibus client account (OM))

LEI processing

It should be noted that the stocks of existing securities will also have to be enriched with the up-to-date LEI of the issuers of these securities. Euroclear is currently collecting these LEIs. These must be updated in coordination with the issuers or their agents, at the update frequency required by this identifier.

ESMA published a memo regarding LEIs on October 9, 2017 (see Bibliography, B. d.).

Since September 2017, for the recording of any new financial instrument, the agent of the issuer must send the LEI of the issuer to the Euroclear ESES CSDs and to Euroclear Bank. Since December 31, 2017, the agent of the issuer shall send to the Euroclear ESES CSDs and to Euroclear Bank the LEIs of all other collective investment undertakings for which they operate as agent.

4.1.1.7 Operational risks

The ESES CSDs and Euroclear Bank will need to identify/monitor the risks on key clients (volumes and deposits). The Terms & Conditions have been adapted to allow the collection of all necessary information on key clients.

4.1.2 Clearstream Banking Luxembourg

4.1.2.1 Banking services

CSDR Art. 59-3, Art. 15-2

CSDR Art. 12-1, Art. 13-1, Art. 14-2, Art. 9 of the RTS on Prudential Requirements for Bankina-Tvæe of Ancillary Services

CSDR Art. 24, Art. 26-1 and-2 (a)

i. Collateralisation of credit exposures

Clearstream's CSDs must ensure that all credit extensions are covered by adequate collaterals and will thus adapt their related payment policy for custody activities, as well as the payment procedures for new syndicated issues, to ensure compliance with the collateral requirement. In addition, Clearstream is required to maintain qualifying liquid resources (QLR) for the currencies with authorised credit.

Impact on participants:

- Stopping non-collateralised credit lines;
- Collateralised credit limits required for the use of advances related to custody activities (coupons, redemptions, etc.) until funds are received by Clearstream;
- Collateralised credit limits required for the issuance of the payment commitment to the common depository, as part of new syndicated issues;
- The availability of credit may vary depending on the currency.

ii. Eligibility and valuation of collaterals

Clearstream's CSDs must adapt their collateral eligibility and valuation approach to meet the enhanced requirements of CSD-R, to further reduce the credit risk exposure of CSDs. The measures will require adjustments in the collateral hierarchy (three-tier classification), concentration limits, price dating and collateral discounting.

Impact on participants:

Adaptations (increase, substitution, diversification) of the collateral portfolios managed with Clearstream

4.1.2.2 Risk management

The existing KYC diligence will be enhanced, by integrating at least:

- an assessment of the risks posed by a participant, particularly in the case of significant volumes;
- An assessment of the risks posed by the clients of the participants.

CSDR Art. 47-1, Art. 67-1

4.1.2.3 *Asset segregation*

Clearstream is already compliant with the provisions of article 38.

CSDR Art. 38-5 and-6

4.1.2.4 *Reconciliations*

It is reminded that participants in CSDs must reconcile on a daily basis with the CSD. With regard to its participants, existing reconciliation measures will be strengthened in order to ensure reconciliation on a daily basis.

CSDR Art. 37-1 and-2

In the event of a reconciliation problem (understood as the patent presumption of overdrafts or debit balances of securities accounts and/or securities creation), Clearstream will suspend the settlement on the relevant ISIN code. It should be noted that this point is being studied at European level in order to ensure suspension consistency at European level.

4.1.2.5 *Book entry form*

The two cases exist today at Clearstream, no impact is to be expected.

CSDR Art. 3-1 and-2

4.1.2.6 *Record-keeping (incl. LEI)*

There is no obligation to transmit the LEI of the participants during the period of transition to CSDR requirements. Thereafter, participants will have to communicate a valid LEI for participants (as well as the renewals of this LEI). As for issuers, the LEI has to be provided for the recording of any new financial instrument or issue renewal.

**CSDR Art. 29
Point 109 of the final
report of ESMA on the
requirements applicable to
CSDs.**

4.1.3 Case of the data Transaction Type (all CSDs authorised under CSD-R)

The 'Transaction type' data is required in the 'Record-keeping' section of CSDR requirements for CSDs, as well as in other sections of the regulation, such as 'Confirmations/Allocations'.

The counterparties and their agents will thus have to provide this data, so that it is available in particular at the level of the central securities depository concerned.

4.1.4 The Segregation Offering (all CSDs authorised under CSD-R)

Only CSD participants have the obligation to offer assets segregation possibilities to their clients. The obligation is not transmitted along the custody chain. For example, a global custodian using a local custodian for the custody of its clients securities in Euroclear France doesn't have the obligation to offer segregation possibilities to said clients.

4.2 Internalised settlement

4.2.1 Introduction

The regulatory framework of the settlement discipline allows the authorities to monitor and penalise the instructions settled late in the books of a central depository located in the European Economic Area. However, it does not allow to track the settlements made in the books of a custodian without any (direct or indirect) account transfer at central depository level. The CSD regulation thus provides that these stakeholders create a quarterly report, containing all instructions settled or failed in their books without having gone through a central depository.

Three main documents set out the framework for these obligations. European regulation 909/2014 on Central Securities Depositories (see Bibliography, A. a.), and the Delegated Regulations 2017/931 and 2017/393 relating to internalised settlement (see Bibliography, C. a. and b.). Based on these umbrella documents, two documents were sent to the European authorities in the context of a Q&A exercise. These documents also provide inputs for interpretation or understanding. They consist in two questionnaires issued by the EBF (European Banking Federation) on the one hand, and by the AFME on the other hand (see Bibliography in Appendix of this document).

In addition, ESMA has published "guidelines" that provide clarification on the implementation of the provisions on reporting requirements for internalised settlements. For convenience purposes, these "guidelines" will be named hereafter "the ESMA guide".

4.2.2 Impact assessment

4.2.2.1 Definitions

Article 1 of the Delegated Regulation 2017/391 specify the definitions of an internalised settlement instruction and of a fails:

‘internalised settlement instruction’ means an instruction by a client of the settlement internaliser to place at the disposal of the recipient an amount of money or to transfer the title to, or interest in, a security or securities by means of a book entry on a register, or otherwise, which is settled by the settlement internaliser in its own books and not through a securities settlement system.

‘failed internalised settlement instruction’ means non-occurrence of settlement, or partial settlement, of a securities transaction at the date agreed by the parties concerned due to a lack of securities or cash, regardless of the underlying cause.

4.2.2.2 Declarant and submitter

As indicated in the ESMA guide (section 5.2, paragraphs 16 and 17, pages 26 and 27), the entity responsible for reporting (the declarant) is the custodian in which books the settlement are internalised:

- Whether or not the custodian is a CSD participant
- Whether or not the custodian delegates its IT and/or Operational processes to a third party: account operator, extended mandate, outsourcing.

The declarant remains fully responsible for the reporting but can delegate the generation and/or submission of the reporting to a third party. Several examples are described in annex of the current document.

The reporting must be sent to the competent authority of the declarant.

It has to be noted that a declarant can send only one reporting for a reporting period.

4.2.2.3 *Competent authorities*

Settlement internalisers shall report to the competent authorities of their place of establishment (article 9-1).

The competent authorities transmit to ESMA the information received from the settlement internalisers.

4.2.2.4 *Reporting modes*

- Custodians have to provide a quarterly aggregated report. This report must be sent within 10 calendar days following the end of each quarter.
- The first period to be reported extends from April 1, 2019 to June 30, 2019. Its reporting will have to be made before July 12, 2019 (first report).

The obligation to report internalised settlements is not part of the Settlement Discipline obligations. Its enforcement is, therefore, not linked to the enforcement of the penalties and buy-in obligations (september 2020).

4.2.2.5 *Case of an institution with several branches, including in third country jurisdiction*

In such a set-up, for its internalised settlements, an institution must create different reports:

- **One** for its own settlement activity in the Member State in which it is established, including that of its branches located in that State, if any.
- **One** per Member State including the settlement activity of its branches in that Member State
- **One** dedicated to the settlement activity of its branches in third countries

An example is provided on page 27 of the ESMA guide:

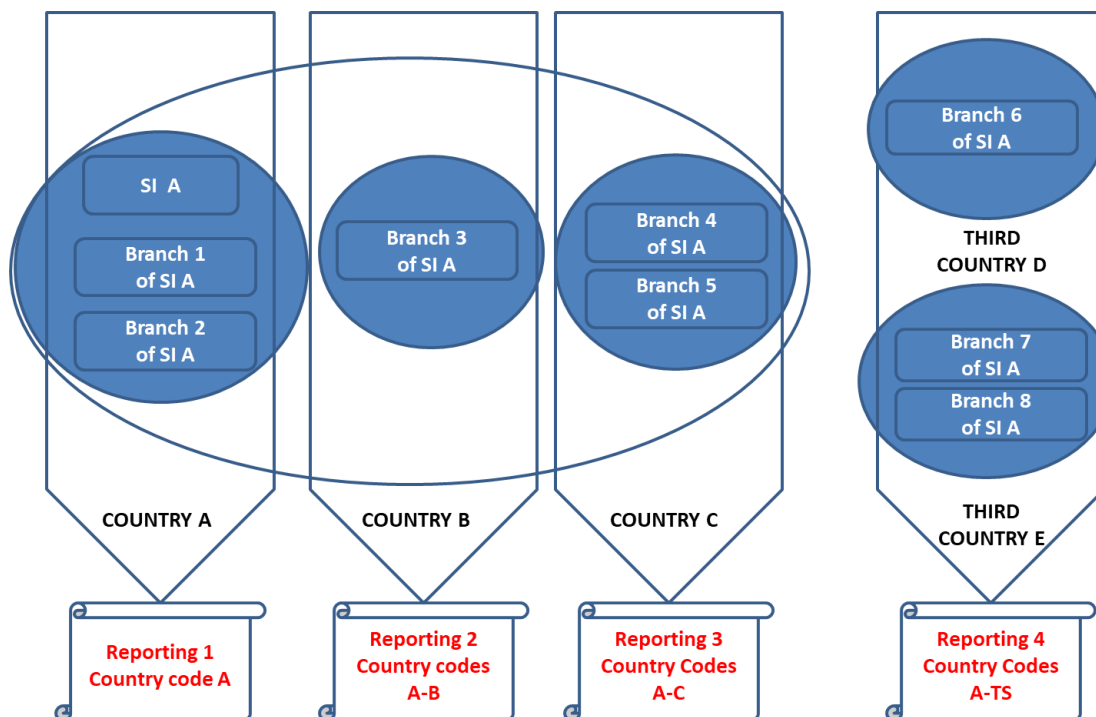
A settlement internaliser established in a Member State A has:

- two branches in State A
- one branch in a Member state B
- two branches in a Member state C
- one branch in a third country D
- two branches in a third country E

This settlement internaliser will have to transmit 4 reports (see diagram):

1. One report covering its settlement activity in Member state A, including the two branches in that State

2. One report for the settlement activity of its branch in country B, mentioning country code B in addition to country code A
3. One report for the settlement activity of the two institutions in country C, mentioning country code C in addition to country code A
4. One report dedicated to the settlement activities in third countries, i.e. the branch in country D and the 2 branches in country E, mentioning country code "TS" (TS for Third Country State) in addition to country code A.



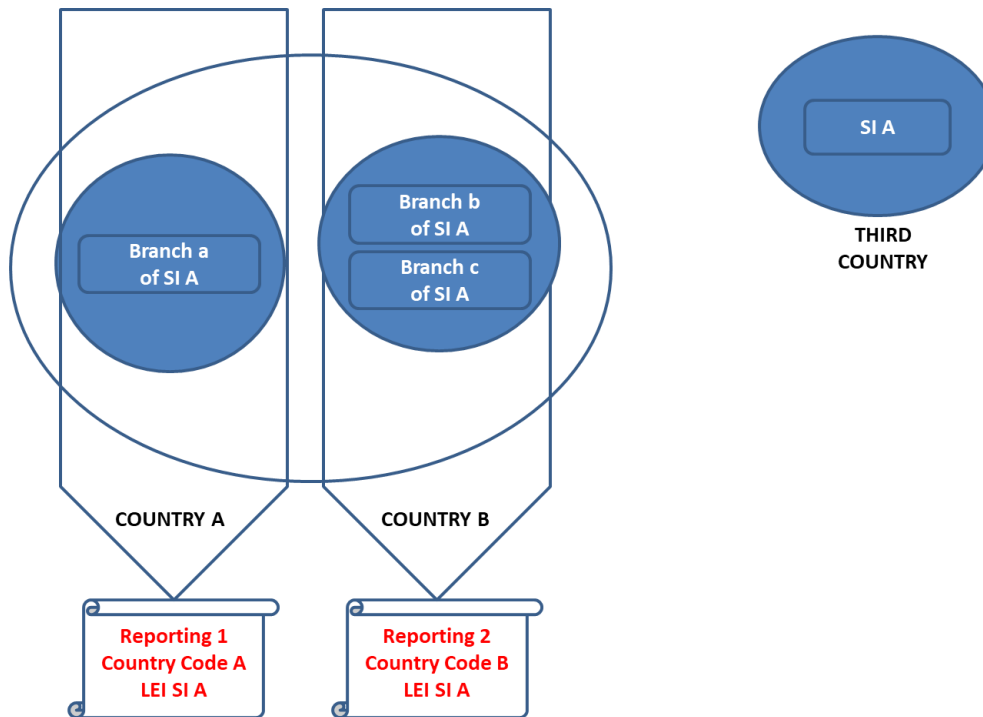
In the case where branches of third country entities are installed in a Member State, the said branches shall report the **internalised settlements** to the competent authorities.

In other words, using the example mentioned on page 27 of the ESMA Implementation Guide, this means that if an entity from a third country has a branch located in a Member State A and two branches in a Member State B: (diagram below)

Where:

- The competent authority of Member State A shall ensure that it receives a report on the internalised settlements of the branch in Member State A
- The competent authority of Member State B shall ensure that it receives a report of the internalised settlements of the two branches in Member State B

In any case, the institution must be identified by the LEI which is associated to it.



4.2.2.6 Types of instruction

In terms of instruction type, based on the regulatory texts and in accordance with the table on page 2 of the EBF document (see Bibliography in Appendix to this document), the concept of internal settlement of an instruction must meet two conditions:

- These are instructions that reflect a transfer of securities from a securities account in the books of an intermediary to another securities account in the books of the said intermediary
- The instruction is applied by the intermediary, at the client's initiative.

These criteria are mentioned in section 5.1, on page 24 of the ESMA Guide.

CLARIFICATIONS:

As initially mentioned, it is appropriate to exclude any simple approach which considers within the reporting scope "any account to account transfer in the books of an intermediary". This vision is too broad and neglects exclusion rules. The concept of instruction "applied by the intermediary at the client's initiative" is one of the mandatory elements for an instruction to be eligible for reporting. This concept is clearly taken up by the EBF.

Thus, a transfer from a PEA (French equity savings plan) to a regular securities account is out of the reporting scope if it does not result from a client's instruction requesting this transfer, but is the result of a purely technical processing (e.g. exclusion of a PEA security made ineligible following a reorganisation corporate action).

Similarly, a pledge of securities in the accounts of an intermediary without transfer of accounts (or sub-accounts) in the books of the intermediary is thus out of the reporting scope.

Finally, changes in legal status resulting in an opening of sub-account or account and the associated transfer would be in the reporting scope.

The corporate actions (such as dividend payment) processed as corporate action on balance with a global settlement at the central depository level are out of the reporting scope. The instruction is applied by the intermediary without the client's initiative.

In addition, the cash instructions related to a delivery of securities (securities/cash dissociated) should be in the reporting scope of CSDR.

Therefore, the following two concepts constitute a first filter of eligibility for reporting requirements:

- internal account to account transfer without going through a CSD or a third party
- resulting from a client's instruction.

The following operations are considered **to be reported**:

- Purchase or sale, including purchase or sale in the primary market¹
- Collateral management operations, including triparty or auto-collateralisation operations
- Securities lending/borrowing
- Repurchase transactions
- Transfers of securities between accounts of different investment funds
- Execution of transfer orders by the settlement internaliser on its own account, to the extent that they result from transactions involving clients
- Transfer of securities between two securities accounts of the same client
- Transfer as part of a collateral or pledge arrangement as defined in points b and c of article 2-1 of Directive 2002/47/EC ("FCD" Financial Collateral Directive)
- Transformations (corporate actions on flows)

The following operations are considered **not to be reported**:

- Corporate actions (on stock)
- Market Claims (corporate actions on flows)
- Issuance of securities (creation of securities)
- Subscription / Redemption of fund units
- Pure cash payments, not related to securities transactions
- Settlement of market transactions leading to a transfer of the market transactions to the CCP or CSD by the trading venue
- Operations netted at CCP level

¹ In this context, the primary market has to be understood as the initial investment in a new issue (IPO, debt issue, etc). As opposed to the secondary market where the financial instruments are exchanged between a seller and a buyer. In this specific situation, it implies that the issuer has its account (issuing account) in the books of the custodian that offers the financial instruments to its clients, also in its own books.

4.2.2.7 *Internalised settlements and nets to settle*

In the guidelines, ESMA addresses the case of netted operations and their inclusion in the scope of the settlements to report:

*The majority of respondents argued that netting should be out of scope as long as the actual settlement takes place on the books of a CSD (even if the settlement instruction itself is a result of different trades being offset, shaped or netted). **However, if the net settlement happens between accounts on the books of the custodian, it should fall into the scope of the reporting.** The respondents argued that in a pairing-off situation the risk element of the transaction would still be settled within the CSD, and the pairing-off helps to reduce risk. One respondent suggested that ESMA should clarify that any aggregation of trading activity prior to the settlement instruction's generation would not be considered in the scope for reporting. Some respondents suggested that "transactions subject to netting as defined in point (k) of Article 2 of Directive 98/26/EC at the level of the settlement internaliser" should instead be added to para.12(g) of the Guidelines included in the CP, with the clarification that only the net difference that is settled at the level of the settlement internaliser should be included. (3.Feedback – point 13)*

*A settlement internaliser should report all settlement instructions which meet the conditions specified in these guidelines, **regardless of any netting performed by that settlement internaliser.** Netting performed by CCPs should not be in the scope of internalised settlement reporting. (guidelines 5.1 §13)*

ESMA indicates that the netting has no impact on the obligation to report and reminds that the settlements to report must be selected based on the definition of an internalised settlement. Replacing several settlement instructions by a single netted settlement instruction doesn't change the nature internal / external of the settlement instructions.

To assess if a net to settle has to be reported, the underlying unit settlement instructions must be analysed:

- Were the instructions settled outside of a CSD settlement system?
- Did the settlements occur between two accounts opened in the CSD books?
- Were the settlement instructions sent by the client?

For example, replacing several settlement instructions to be sent to a CSD by a single netted settlement instruction to be sent to said CSD doesn't change the external nature of the settlement instructions. The netted settlement instruction is out of scope of the reporting obligation as the origin settlement instructions. For that matter, the account "counterparty" of the client account is an account used for external settlements. Furthermore, the client has not requested its custodian to settle its settlement instructions against another client of said custodian (the accounts used for external settlements are not client accounts).

4.2.2.8 Geographical scope

In terms of geographical scope, based on the regulation and in accordance with the table on page 2 of the EBF document (see Bibliography in Appendix to this document), the concept of internal settlement relates to securities whose intended place of settlement is a central depository of the European Economic Area, with the reservations and clarifications mentioned in section f below.

CLARIFICATION:

The geographical scope of application covers the EEA (European Economic Area). The texts (ITS and RTS) mention in their subtitle "Text with EEA relevance" confirming the geographical scope of application. At the time of the writing of the current document, the EEA comprises the European Union countries and the 3 following EFTA countries: Iceland, Liechtenstein and Norway.

4.2.2.9 Financial instruments:

ESMA states that the instruments covered by the provisions relating to the reporting obligations of internalised settlements are the financial instruments for which a central depository of the European Union acts as issuer CSD or as investor CSD (paragraph 14 page 26 of the ESMA guide).

It is indeed mentioned that the following instruments should be considered within the scope of the provisions on internalised settlements:

- Financial instruments that are initially issued or centrally recorded by a central securities depository authorised to conduct its business in the European Union, i.e. any security for which the central depository acts in an issuer CSD capacity.
- Financial instruments which are settled in a central depository of the European Union and for which said central depository acts in its investor CSD capacity.
- By extension, any financial instrument which does not fit in the categories listed above but which meets the conditions stated in the ESMA guidelines.

4.2.2.10 Concept of place of settlement

The reference place of settlement (PSET) of a security is one of the factors determining whether or not the reporting obligations apply. At the suggestion of the EBF, the scope of financial instruments subject to internalised settlement is limited to those eligible for settlement in a Securities Settlement System (SSS) of a central depository approved under CSDR.

As a result:

- securities admitted to the operations of an investor CSD are within the scope of application.
- Non-transferable securities subject to a transfer order ('Ordre de Mouvement' or 'ODM' in French) do not fall within the reporting obligation under CSDR in the event of an internalised settlement on this type of instrument.

The use of the PSET is not sufficient for ESMA, which sees it as a way to remove the responsibility from the settlement internaliser and fears that the PSET may not always be specified by the client.

In fact, this does not preclude the use of the PSET but means that the settlement internaliser verifies its relevance to the instruction provided by the client and enriches or corrects it based on its own settlement and custody rules.

The settlement internaliser will ultimately define the elements to be reported according to the ESMA rules and to the place of settlement deemed relevant to an equivalent settlement that would have taken place in a central depository.

Note: In the case of money market instruments (short-term debt securities) issued by an institution and recorded in its books, the application of the PSET-based rule means that such security, whose reference PSET is a CSD of EEA, falls within the scope of the reporting obligation.

4.2.2.11 Failed Instruction ('fail')

In case of fail, the ISD (Intended Settlement Date) must be compared with the date of application of the settlement within the institution (comparison between actual settlement date and Intended Settlement Date).

4.2.2.12 Format

Regulation (EU) No. 909/2014 requires settlement internalisers and their competent authorities to transmit quarterly information and reports based on standard formats (ISO). The settlement internaliser shall use the template specified in Appendix 1 of this regulation, in compliance with the provisions of article 9-1 of Regulation (EU) No. 909/2014.

The ESMA Guide states, in section 5.4 page 29, that entities shall submit their reports in XML format based on the ISO 20022 message definitions published by ESMA on the 10th of October 2018.

4.2.2.13 Data

The report provided for in Article 9(1) of CSDR ((EU) No. 909/2014) shall contain the data provided for in article 2 of the delegated acts relating to settlement internalisation (*see Appendix*).

The volume data and values are aggregated and stated in euros. So there is no detailed report required, such as line-by-line instructions.

The following should be reported (see page 28 of the ESMA Guide):

- the first two characters of the ISIN code,
- the LEI of the Issuer CSD corresponding to the relevant security (article 2-1 delegated regulation 2017/391). If necessary several Issuer CSDs may be mentioned,
- the country code of the Issuer CSD is deduced by ESMA and not reported by the settlement internaliser.
- all instructions leading to an internalised settlement. Thus an internalised settlement implies reporting both receipt and delivery (two instructions are settled).
- The volumes are stated in number of settled instructions
- The settlement instruction failed during a reporting period must be reported as such for each of the failed days observed. If they are settled during the same period, they must also be reported for their settlement as settled operation.

ESMA provides the following example in its guidelines (page 28)

If during a quarter an internalised settlement instruction with a value of €100 fails to settle for 3 days, and then is settled, it should be reported as follows:

Settled operations: 2 for a value of €200. For a settlement, two instructions of €100 had to match.

Failed operations: 6 for a value of €600 (i.e. 2 instructions x 3 failed days x €100)

For a total of 8 operations for a value of €800. (consistency check)

Settled		Failed		Total	
Volume	Value (EUR)	Volume	Value (EUR)	Volume	Value (EUR)
2	200	6	600	8	800

Source: ESMA Guide Table page 28

4.3 Confirmations/Allocations

The technical standards of the Settlement Discipline section of the CSD regulation anticipate matching and settlement difficulties by recommending practices for affirmation and communication of allocations between investment firms and their professional clients.

These recommendations focus on the following elements:

- Standardisation of the data exchanged between investment firms and their professional clients, to be exchanged via international and open communication protocols, messaging and codification standards.
 - Transaction type
 - ISIN
 - Delivery or receipt of instruments or cash
 - Nominal value for debt instruments, quantity for other financial instruments
 - Transaction date.
 - Transaction price of the instrument
 - Currency in which the transaction is stated
 - Intended settlement date
 - Total amount of cash to pay or receive
 - The ID or the entity where the securities are held in custody
 - The ID or the entity where the cash is held
 - The name and ID of the securities account and/or cash account
- Reduced timeline to confirm and communicate the allocations:
 - The affirmation and allocation must be achieved at trading date, except when the two counterparties are located in time zones with a difference of 2 hours or more, or when the orders are executed after 4:00 pm CET; in such cases, the deadline is T+1 12:00 pm CET (T means trading date)
 - The investment firm has 2 hours to confirm the correct receipt of the allocation/confirmation to its professional client.

The French financial institutions have identified the following impacts:

- Despite the evolutions due to implementation of the settlement cycle shortened to T+2, some investors will have to adjust their confirmation/allocation process in order to support a processing within the day or at T+1 noon.
- For the processing of confirmations and allocations on equity and debt securities, the market recommends to the institutions and their professional clients to use electronic channels.
- In terms of data to be transmitted, the impact seems limited to the data 'Type of transactions' (Purchase or sale of securities, Collateral management operations, Securities lending and securities borrowing, Repurchase transactions, Other securities transactions) which, although not a matching criterion, is a data that must be transmitted in all confirmations.

4.4 Settlement discipline: Settlement fails penalty scheme

MiFIDII Level 2 texts laid out the obligation for investment firms to implement measures to prevent the unauthorised use of clients financial instruments and to prevent fails: financial instruments borrowing, settlement monitoring before and after the intended settlement date, and corrective measures (it has to be noted that such obligations were already written in French Law in the regulatory framework for custody account keepers).

The CSD regulation and the technical standards proposed by ESMA complete the measures by imposing penalties on settlement fails. The penalty model selected by the regulator has the following characteristics:

- One penalty applied to each instruction;
- Triggered by lack of securities or lack of cash;
- On ad valorem basis using a reference price;
- Penalty paid in full to the failed counterparty;
- Penalty calculation centralised at CSD level;
- Penalty collection and distribution management at CSD and CCP level;
- Operating costs of the penalty management system paid separately.

The model planned under CSDR is intended to have a deterrent effect, and the penalty rates will vary according to the instruments (according to their liquidity for instance).

4.4.1 General impacts

The participants of each CSD/ICSD will have to implement a specific penalty management process:

- Daily monitoring of the penalty file sent by each CSD/ICSD, reconciliation with fails and triggering of claims when necessary;
- Management and provisioning of the accounts dedicated to the payment of penalties in due time;
- Monthly monitoring of penalty billing, reconciliation with daily files;
- Monthly monitoring of penalty payment, according to the mode of collection and billing chosen by the CSD/ICSD (net/detail, collection date).
- Breakdown of some settlement instructions and recalculation of penalties in order to pass on to the clients the billed penalties.

As a reminder, each participant of a CSD/ICSD has the responsibility to define its own passing on policy towards its clients.

Participants affiliated with several CSDs and/or CCPs could have to manage penalties originated from multiple sources, with potentially different calculation modalities, information exchanged, calendars...

Nevertheless, it has to be noted that:

- Penalties on Fails for T2S flows will be calculated by the T2S penalties calculation engine (cf EMSA Q&A)
- Penalties on Fails for non T2S flows will not be calculated by the T2S penalties calculation engine
- The definition of the messages to use for penalties is ongoing based on ISO formats 15022 and 20022; a participant could receive ISO 20022 directly from T2S as a DCP and/or ISO 15022 or 20022 from a CSD²

² Some CSDs don't intend to provide ISO 15022 messages to their participants for penalties

In order to better harmonise the processes, and facilitate cross-CSD reconciliation, ECSDA is currently working on a framework of good practices that would be adopted by all CSDs subject to CSDR (same messages, same life cycle, same detection principles...)

Beyond a participant “standard” penalties management practices, a few cases should be highlighted.

For example:

- An institution participant of a CSD A and using the services of a local custodian for a CSD B (or using the services of a 3rd party account operator for the management of its account in a CSD): the institution will exchange information with both CSD A and its service provider for CSD B; the institution will be charged penalties as the defaulting party for a transaction settled directly in the CSD; for the transaction settled via a local custodian, it will depend on the penalties scheme the local custodian will adopt.
- A clearer using the services of a settlement agent for the settlement of its clearing activity in a CSD: the penalties for the CCP will be charged directly to the clearer whereas the penalties for the settlements between the clearer and custody account keepers will be charged to its settlement agent; the latter will have to put arrangements in place with the clearer to charge back the penalties to said clearer.

It has to be highlighted that the delegated act provides for penalties charged for settlement instructions matched after the intended settlement date (aka late matching penalties) to be charged to the institution which has last sent or modified the settlement instruction, even if they are not the faulty counterparty.

For example: upon disagreement on the amount between participant A and participant B, A makes a goodwill gesture and sends, after the intended settlement date, a new instruction with the amount set by B; A will be the penalised participant.

4.4.2 Scope of Financial Instruments

According to the CSD regulation and the ESMA Q&A, the financial instruments in scope have the following characteristics:

- These are transferable securities, money market instruments, units in collective investment undertakings or emission allowances;
- They are either admitted to trading or traded on a trading venue, or cleared by a central counterparty.
- The units in collective investment undertakings which are neither admitted to a trading venue (TV) nor cleared by a CCP are not in the penalty scope

4.4.3 Scope of instructions

An instruction is to be penalised in the following cases:

- if it relates to a financial instrument which is in the penalty scope;
- and if it is not completely settled on the relevant date (intended settlement date);
- and if it is matched (the delegated regulation 2018/1229 imposes, with some exceptions, the matching of instructions before settlement).

The scope of 'penalisable' instructions also includes:

- instructions in 'On hold' status;
- instructions sent or matched after the intended settlement date.

However, the detailed typology of the instructions to be penalised or not (e.g. instructions resulting from corporate actions, collateral trading, etc.) are under discussion with the ESMA.

Currently, only corporate actions on positions (type 'CORP') and T2S technical realignments are considered out of scope of penalties in T2S calculation engine.

Note: In T2S, the platform allows to condition the settlement of an instruction 1 to that of an instruction 2. If instruction 2 fails, instruction 1 will not be settled and then both of them will be penalised.

4.4.4 Penalty calculation

The penalties are calculated:

- at unit level (settlement instruction);
- for each business day.

Point of interest: In case of instructions not eligible to partial settlement, at the request of the securities recipient, the instruction shall be subject to penalties for all securities to be delivered, even if the participant can make a partial delivery (part of the securities are in stock)

*E.g. receipt of 800 securities (ok)
 receipt of 200 securities (fail)
 delivery of 1,000 securities with an opt-out requested by the recipient (fail)*

⇒ the participant will pay a penalty on the 1,000 securities and will receive a compensation on the 200 securities.

The calculation formula has always the following structure (cf ESMA Q&A):

Basis * Rate

Where:

- The basis is equal to the failing quantity of a financial instrument * the reference price of the financial instrument (delegated regulation 2017/389), except where the failing settlement instruction has a null quantity or for delivery with payment / receipt with payment settlement instructions (in such cases, the basis is equal to the failing amount),
- The rate is defined by the delegated regulation 2017/389, according to the type of financial instruments or the currency of the cash amount. The rate to apply depends on the root cause of the fails and on the type of settlement instruction. For example, if the participant receiving the financial instruments is at the origin of the fails, the rate linked to the payment currency will be used, unless the settlement instruction is free of payment in which case the rate linked to the financial instrument will be used.

→ Two points of interest:

- A double penalty is charged to Delivery with payment / Receipt with payment (DWP/RWP) settlement instructions
- The rate to be used for SME markets depends on the contents of the field 'Trading Place' in the settlement instructions (cf ESMA Q&A)

4.4.5 Penalties correction

The number of penalties modification should be low. The ESMA is expected to provide more details regarding the process (perhaps, via the Q&A). Some scenarii (such as the bankruptcy of a participant, the suspension of a financial instrument) could require only a posteriori reports to the regulators.

4.4.6 Cross Border Settlements

Cross Border settlements occur between:

- A T2S CSD and a non-T2S CSD
- Two non-T2S CSDs

The principle is that the place of settlement indicated in the settlement instruction defines which CSD is in charge of the penalties calculation. Said CSD will provide all required information to its counterparty CSD, which in turn will provide them to its participant.

The settlement scenarii have been approved by the ESMA but remain to be made official.

The ECSDA Settlement Fails Penalties framework will bring more clarification regarding penalties management for Cross Border settlements.

4.4.7 Calculation formulas

The calculation formulas are as follows, depending on the type of settlement instruction and the reason for the non-settlement:

Summary of the various penalty cases (based on the work of the Penalties Task Force under the umbrella of ECB)

Base = Reference price * Quantity

where quantity is :

- the remaining quantity in case of lack of securities or cash
- the whole quantity in case of instruction on hold

Base = Amount when quantity = 0

As proposed in the T2S penalty mechanism - January 2017

lack of securities	lack of cash
double penalty	base = amount

formula	what is to be penalised?	reason	A	B	reason	what is to be penalised?	formula
Base*rate sec	non delivery	lack of securities	DVP	RVP	lack of cash	non payment	Base*discount rate
Base*rate sec	non delivery	instruction on hold			instruction on hold	non receptionsec	Base*rate sec
Base*rate sec	non delivery	linked to an unsettled inst.			linked to an unsettled inst.	non receptionsec	Base*rate sec
Base*rate sec	non delivery	late instruction			late instruction	non receptionsec	Base*rate sec
Base*rate sec	non delivery	lack of securities	DFP	RFP			
Base*rate sec	non delivery	instruction on hold			instruction on hold	non receptionsec	Base*rate sec
Base*rate sec	non delivery	linked to an unsettled inst.			linked to an unsettled inst.	non receptionsec	Base*rate sec
Base*rate sec	non delivery	late instruction			late instruction	non receptionsec	Base*rate sec
(1) Base*rate + amount*rate	non delivery + non payment	lack of securities	DWP	RWP			
(1) Base*rate + amount*rate	non delivery + non payment	lack of cash					
(1) Base*rate + amount*rate	non delivery + non payment	instruction on hold			instruction on hold	non reception (sec + cash)	Base*rate + amount*rate (1)
(1) Base*rate + amount*rate	non delivery + non payment	linked to an unsettled inst.			linked to an unsettled inst.	non reception (sec + cash)	Base*rate + amount*rate (1)
(1) Base*rate + amount*rate	non delivery + non payment	late instruction	late instruction	non reception (sec + cash)	Base*rate + amount*rate (1)		
Amount*discount rate	non payment	lack of cash	DPFOD	CPFOD			
Amount*discount rate	non payment	instruction on hold			instruction on hold	non reception cash	Amount*rate cash
Amount*discount rate	non payment	linked to an unsettled inst.			linked to an unsettled inst.	non reception cash	Amount*rate cash
Amount*discount rate	non payment	late instruction			late instruction	non reception cash	Amount*rate cash

(1) : still under discussion, the type of the rate used; either the rate sec or the discount rate

4.5 Settlement discipline: Mandatory buy-in procedures

This topic will be covered in a later version of the document, following the results of the work undertaken by european professional associations on buy-ins, pending some clarification from the regulator.

5 Appendices

5.1 Objectives and mandates of the GLF CSDR Group

5.1.1 Objectives

- a. Propose a position of the French market on the impacts of the CSD regulation on market practices.
- b. The CSDR impact assessment will be consolidated in a specifications document.

5.1.2 Mandates

The GLF, as a transversal group of AFTI, is in charge of coordinating this work with the various AFTI groups.

- The main AFTI groups concerned are: Fixed Income and Collateral workgroup ("MOC") – Equities – Custody – Issuers – International Observatory – Flow and Stock. Each of these groups is represented at GLF via a specific point of contact.
- Depending on the assessments carried out, other thematic groups of AFTI may be contacted.

The major banking institutions of the French market, as well as the market infrastructures (Stock Exchange, CCP, CSD/ICSD), are represented at GLF via at least one point of contact.

The following key topics, and their impacts for the participants of the French market, will be addressed in the specifications:

- Impacts arising from the CSD and ICSD license under CSDR (including the impacts of the 'limited-purpose bank')
- Fails penalty scheme
- Buy-in procedure
- Internalised settlement

A coordination will be ensured:

- with other associations of the French market: AMAFI, AFG, ANSA
- with other work carried out in Europe on these topics: especially the ECB work on penalties, the AFME's work, the ICMA's work
- market infrastructures will ensure the coordination with the work carried out in their professional associations (EACH, ECSDA)

5.2 List of participants in the GLF CSDR

Leader	Company
Tibi Marc	BP2S

Rapporteur	Company
Corona Nathalie	Cognizant Consulting
Dubrau François	Cognizant Consulting

Permanents	Company
Bachelier Adeline	Banque de France
Barthelemy Lionel	CACEIS
Berthe Christophe	CDC
Bey Eric	Euronext
Bonduelle Sylvie	SGSS
Chaput Michel	Citigroup
Colladon Pierre	SGSS
Darracq Kevin	HSBC
Di Lorenzo Italo	Clearstream
Dromain Amélie	Deutsche Bank
Facon Pauline	Banque de France
Gandois Jean-Pierre	HSBC
Guéorguieva Luba	CM-CIC
Janssens Paul	SWIFT
Joannet Mathilde	Euroclear
Juy Delphine	Natixis
Khirat Mourad	Natixis
Mairesse Anne	LCH Clearnet
Marcel Fleury Vincent	HSBC
Marie Dominique	Natixis
Marraud Brice	CACEIS
Mathieu Muriel	CACEIS
Planet Frederic	Natixis
Truskowski Caroline	BP2S
Observer	
Degryse Michel	AMF

5.3 FAQ

ID	Topic	Question	Requester	Answer	Status
Affirmations/Confirmations					
A1	Affirmation/Confirmation platforms	Will there be new service providers in this market following the new requirements under CSDR?	Equities	<p>It will be up to each institution to comply with the new rules. The specifications will only mention the new requirements of CSDR, without detailing any possible technical solutions.</p> <p>However, the names of some service providers have been mentioned by AMAFI: Traiana, Omgeo CTM, Fixallocator, SWIFT</p>	Closed
A2	OTC transactions	(At least debt securities) When the transactions are not affirmed/confirmed via venues, what are the impacts to be expected?	Equities	<p>At least to be able to affirm/allocate via another channel these transactions while complying with the regulatory requirements.</p> <p>For professional clients, AMAFI recommends banning the use of a non-digital channel.</p>	Closed
A3	Scope	Can it be confirmed that the requirements on affirmation / confirmation flows do not have any specificities according to the asset classes?	GLF CSDR	<p><i>Comment: The scope is that of the financial instruments - article 5(1) of CSDR:</i></p> <p><i>transferable securities, money market instruments, units in collective investment undertakings or emission allowances / No additional distinctions</i></p> <p><i>The differences relate to the type of client (pro / non-pro) and the feasibility (time zone, end of day)</i></p> <p><i>So this is a subset of the financial instruments.</i></p>	Closed

ID	Topic	Question	Requester	Answer	Status
A4	Sanctions	What are the sanctions in case of failure to comply with the affirmation/confirmation rules?	GLF CSDR	There is nothing specific in the regulation on the sanction scheme; but it is the duty of institutions to comply with the regulation (the regulator has the power to enforce sanctions).	Closed
Impacts of the CSD & ICSD license					
I1	Messaging	Specify the impacts on the existing proprietary messages (e.g. SBI) <i>Reference: Article 35 of CSDR and question 4 of ESMA Q&A</i>	Equities	SBI is involved before the settlement, it is thus out of scope. There is no expected impact on SBI messaging.	Closed
I2	Default of a participant	Are there any changes to be planned as a result of the license under CSDR?	Equities	In case of a bankruptcy which would lead to a default, there is no impact to be expected. Nevertheless the CSDs will change the rulebooks to describe this case.	Closed
I3	Record-keeping	Confirm that the LEI does not have to be transmitted in the instructions - Confirm the need to provide the LEI of the issuer and the implementation date (September 2017, March 2018 at Euroclear side?)	GLF CSDR	Settlement Instructions The LEI of the participant is mandatory (especially under MIFIR from January 3, 2018); on the other hand, there is no obligation to transmit the LEI of the participant's clients in the instructions. Note that T2S has found a way to transmit the LEI when it is available but it is not a mandatory field. Issuer's LEI In case of a new issue, Euroclear has confirmed that until the authorisation date, only a proof of the request for LEI is required. From October 1, 2017, Euroclear wants the issuer's LEI to be obtained beforehand; a	Closed

ID	Topic	Question	Requester	Answer	Status
				tolerance will be observed, and the admission request will not be rejected if the LEI has not been obtained yet. Note that for some funds which are not eligible to CSDR, the LEI is not necessary.	
14	Record-keeping	From Q2 2019, should the LEI be transmitted for any instruction (Article 11 – 1 ITS and Appendix 4 and Article 54 of RTS and Q&A of March 31, 2017 specifying the entry into force upon the implementation of the settlement discipline)?	Flow and Stocks	See 13	-
15	Asset segregation	Via which process will the CSDs/ICSDs inform their participants of the content of Article 38 (choice of omnibus/individual segregation and associated costs and risks)?	GLF CSDR	All information on account segregation is available in the "Rights of Clients to Securities deposited in the ESES CSDs" document, updated in July 2017. Associated costs are available in "ESES Tariff brochure"	Closed
16	Reconciliations	What are the expectations of CSDs/ICSDs towards participants in terms of daily reconciliation, particularly on the issuer/fund side?	GLF CSDR	CSDs/ICSDs are not required to check the participants' practices on this matter	Closed
17	Suspension of settlement in case of a reconciliation problem	What is the process for ADR/GDR, since the source CSD is most often not subject to CSDR	Fixed Income and Collateral	Euroclear Action	Open
18	Operational risk	'Key participant' concept: detail the information required from these participants and the activity monitoring	GLF CSDR	The information required by each CSD on its key participants remains discretionary and will not be harmonised among CSDs.	Closed
19	Operational risk	Non-CSD: Confirm that the participants' clients must also provide the same type of information as a participant in CSDs	GLF CSDR	No information on the participants' clients is requested by the CSDs & ICSDs at this stage.	Closed

ID	Topic	Question	Requester	Answer	Status
I10	Record-keeping	For money market instruments, , how will it be checked that the issuer has a valid LEI, knowing that several ESES members can issue money market instruments for the same issuer?	GLF CSDR	<p>The validity of the issuer's LEI is not checked on the fly.</p> <p>In case of automatic request: the issuer's LEI would be checked later.</p> <p>For the stock of existing instruments, and subject to subsequent confirmation, a check would occur at a fixed frequency, and at least 1 to 2 months before the LEI reaches its expiration date, generating a warning and a reminder to the Issuer's Agent.</p>	Closed
Fails-related penalties					
P1	Scope of enforcement	Are "On Hold" instructions included in the scope of enforcement (and more generally in the Settlement Discipline section)?	Fixed Income and Collateral	Any on hold and matched instruction that has exceeded the agreed intended settlement date will be subject to the settlement discipline section.	Closed
P2	Scope of enforcement	Are repos and French 'pensions livrées' included in the scope of enforcement?	Fixed Income and Collateral	<p>Yes.</p> <p><i>Note: The link with the life cycle is only for buy-ins</i></p>	Closed
	Scope of enforcement	<p>Exclusion:</p> <ul style="list-style-type: none"> - which operations are excluded from the scope? - specifically which operations in terms of collateral? 	Fixed Income and Collateral	<p>To be detailed in the specifications in a later version</p> <p><i>Comment: at this stage, the text does not contain any exemption, beyond that related to the financial instrument itself</i></p>	Open
P3	Scope of enforcement	<p>Does the penalty scheme under CSDR replace the various penalty schemes currently in force at various CSDs (fail-related and also late instruction-related penalties)?</p> <p>If not, which ones would be maintained?</p>	Fixed Income and Collateral	The ESES CSDs have confirmed that their current scheme will be completely replaced by the CSDR penalties scheme.	Closed

ID	Topic	Question	Requester	Answer	Status
P4	Scope of enforcement	<p>In case of a chain of transactions, will all the failed transactions be subject to a penalty?</p> <p><i>If possible, provide a description of the process for determining the transaction(s) to be penalised in a diagram</i></p>	Fixed Income and Collateral	<p>Yes, considering that the penalty applies to the transaction, any failed transaction will be subject to penalty.</p> <p><i>It should be noted that the concept of settlement chain does not exist in the eyes of a CSD (except when the settlements are linked). So the penalty system only sees individual instructions to be penalised</i></p>	Closed
P5	Calculation methods and rate	Which valuation method should be used in the fails calculation (reference price, etc.) ?	Fixed Income and Collateral	Closing price of the previous day	Closed
P6	Calculation methods and rate	When it comes to a closing price, which market is considered?	Fixed Income and Collateral	Proposition: closing price on the reference market of the financial instrument. The identification of the reference market of the financial market, especially when issued outside of the EU, remains an open question which has been raised to the regulator.	Open
P7	Calculation methods and rate	<p>Could we have some numerical examples of penalty calculation on a particular transaction? E.g.</p> <ul style="list-style-type: none"> - a simple case, for example of a May 25, 2027 OAT (government bond) – very liquid, between two participants in the same CSD, - Another case of a fail on an OAT between 2 participants in two different CSDs. - Another case of a fail because of a lack of cash 	Fixed Income and Collateral	To be detailed in the specifications in a later version	Open

ID	Topic	Question	Requester	Answer	Status
P8	Calculation methods and rate	In case of default due to a lack of cash, is the rate applied the Eonia rate (with floor at zero) or the ECB lending facility rate?	Fixed Income and Collateral	To be detailed in the specifications in a later version	Open
P9	Calculation methods and rate	The penalty calculation takes into account the business days only. What about Target days? Are May 1, Good Friday and Easter Monday considered as weekends?	Fixed Income and Collateral	Penalties are calculated by business day, i.e. excluding weekends and non-Target days	Closed
P10	Payment process	What is the propagation of the penalty system between stakeholders in the same chain of transactions?	Fixed Income and Collateral	As the penalty applies to any failed transaction, the propagation of the penalty will follow the chain of transactions.	Closed
P11	Payment process	<p>If a client must receive securities for redelivery, but the purchase is unmatched because the counterparty is not in place, the client will bear the penalties on the sale, which is a failed security sale.</p> <p>If the counterparty is in place 5 days later, the counterparty should pay the penalties retroactively; in this case, will the client be reimbursed for the total amount of the penalties borne due to this fail?</p>	Fixed Income and Collateral	<p>The penalty scheme is a system of penalties and not compensation; which means that its objective is to penalise the defaulter and not to compensate a counterparty which would have suffered from the non-delivery of securities. In this example, the counterparty which enters its instructions 5 days after, retroactively, will have to bear the penalties retroactively</p> <p><i>Comment: The purpose is to ensure maximum neutrality for the party wrongly penalised.</i></p> <p><i>The T2S mechanism provides for the calculation of penalties over the past days using the reference price of the day in question. The only limitations are a 3-month anteriority and, of course, if the quantities are not the same.</i></p>	Closed
P12	Payment process	How often would the CSD collect the penalties? (Daily? Monthly?)	Fixed Income and Collateral	The penalties will be collected on a monthly basis. However,	Closed

ID	Topic	Question	Requester	Answer	Status
				the information on the penalised transactions (and the amount of the day's penalty) must be received daily	
P13	Payment process	How will the collection and application of penalties be carried out for participants (debit and credit)? Will they be included in the monthly invoice or will they be part of a separate process?	Fixed Income and Collateral	The penalty collection / redistribution process will not be included in the monthly invoice, and will be subject to a specific process. To be detailed in the specifications related to Euroclear France	Open
P14	Payment process	How can be found the actual defaulting client, to which the penalty should be charged?	Equities	It is up to each CSD participant to have their own internal system in order to allocate the penalties to their clients in a fair way	Closed
P15	Other	What will be the operating/development costs of the penalty tools?	Equities	Euroclear: this information will only be available at a later stage.	Open
P16	Other	With CSDR, the use of partial becomes "mandatory" and overrides the fact that the client mentioned in its instruction that it did not want any partial (NPAR); in this case, the client can receive a part of the securities, but if its sale is in "hold" status, there will be no automatic partial in T2S on the latter? This may lead the custodian to make an internal development to create this partial on the sale (costly for them), or the 2 counterparties to agree with each other to cancel the original line and re-instruct 2 legs (tedious and manual).	Fixed Income and Collateral	Partial is the default option, which means that a participant can refuse it (opt-out). On the other hand, this decision may have consequences in terms of penalties; for example, C expects 100 securities from A, 900 securities from B and must re-deliver the 1,000 securities to D which made an opt-out. C receives the 900 but not the 100. A will be penalised for the 100, C for the 1,000 and compensated for the 100 (plus C will have paid the 900). The exercise of the opt-out is only done in view of triggering a buy-in (it would be abnormal for C to be redeemed for 1,000	Closed

ID	Topic	Question	Requester	Answer	Status
				securities while there are 900 in stock).	
P17	Scope	Can it be confirmed that the scope of enforcement of the penalties covers all asset classes and transactions types (Purchase/Sale; Lending/Borrowing)?	GLF CSDR	<i>Comment: The starting point must be the financial instrument. Is it subject to penalties or not? If the answer is yes, then a settlement instruction matched and not fully settled at the right date is to be penalised (exceptions will be very rare; for now it is essentially corporate actions on stock)</i>	Open
P18	Calculation methods	Can the penalty calculation methods be different depending on the CSDs? If yes, what will be the impacts for the participants?	GLF CSDR	In theory no, but to be sure, a rule book of best practices intended for all CSDs subject to CSDR is being reviewed by ECSDA.	Closed
P19	Calculation methods	What visibility will the participants have on the calculation methods, especially for those who wish to pass them on to their own clients?	GLF CSDR	On a daily basis, the clients will receive a list of their penalty amounts for the day, with calculation details.	Closed
P20	Reporting	What will be the format of the daily reporting on penalties? is the format free? What will be the impacts to be expected by participants in the way this data is integrated?	GLF CSDR	The message formats should be aligned. The T2S CSDR TF is working on the definition of messages. They will have to be included in the rule book of best practices intended for all CSDs subject to CSDR, which is being drafted by ECSDA.	Closed
P21	Reporting	Can you confirm that participants are not required to reconcile the penalty data on a daily basis?	Fixed Income and Collateral	There is no obligation for the CSD's clients	Closed
P22	Calculation methods	Is there a time limit set by CSDR to challenge the penalties after they have been sent by the CSDs? <i>Comment: T2S provides for a time limit</i>	Fixed Income and Collateral	No time limit is set by the regulation. A rule book of market practices intended for all CSDs subject to CSDR is being drafted by	Closed

ID	Topic	Question	Requester	Answer	Status
				ECSDA, and must cover this subject.	
P23	Billing	With respect to monthly billing, when will it be sent: on the last day of the month? What will be the format?	Fixed Income and Collateral	A rule book of best practices intended for all CSDs subject to CSDR is being drafted by ECSDA, and must cover this subject.	Open
P24	Scope	Which T2S statuses will be scanned to be penalised: Is this everything in Pending or only some Pending cases, depending on the reason for the fail? And also depending on the type of instruction, e.g. CORP is not penalised.	GLF CSDR	At the closing time of settlement day (4:00 p.m, 6:00 p.m, and end of the BATM window), T2S will generate a report of instructions in PENF status to be subjected to penalty. A change request was raised to T2S to be able to do so.	Closed
P25	Calculation	As the institutions will have to break down some settlement instructions and recalculate the penalties to pass them on to their clients, is it planned to share the penalty rates through the financial data vendors, to feed the repositories?	GLF CSDR	Participants will have all the necessary information (see the message drafts written by the T2S TF) to break down / assign penalties to their clients Nevertheless, the level of details to be provided regarding the reference data used for a fails remains an open topic.	Closed
P26	Penalty taxation	If it is a client portfolio transfer, the penalty may fall to the end client (Individual or Entity). What would be the tax to apply to these payments?	GLF CSDR	The topic of penalty taxation was initiated by the T2S TF to ESMA	Open
P27	Calculation	The calculation basis would be that of the closing price of the value if the transfer is Delivery versus Payment or Free of Payment. Will the closing price always be that of the financial instruments main market?	GLF CSDR		Open
P28	Calculation	Case of money market instruments: As the transferable debt security has no trading price, should the nominal value	GLF CSDR	.	Open

ID	Topic	Question	Requester	Answer	Status
		be taken as the basis, i.e. the FMT amount of the fail instruction?			
P29	Scope	In case of internal transfers of an affiliate (conversion, change of account type, etc.), can the fails on these transfers be penalised ('OWNI' instruction type of for example)?	GLF CSDR	Yes, there is no exception on these transfers	Closed
Buy-ins					
B1	Cash compensation	To calculate the cash compensation, how to determine the most liquid market for calculating the "market value"?	Fixed Income and Collateral	To be detailed in the specifications in a later version	Open
B2	Process	When the buy-in trigger date has been reached, what action should be taken? Should we wait to be informed by the CSD, the CCP?	Fixed Income and Collateral	<i>The delegated regulation adopts ESMA proposition to consider that a buy-in has to be triggered by the parties at transaction level,</i>	Closed
B3	Reporting	What reporting should be carried out by the participants following the triggering of a buy-in, with what content and which recipients?	Fixed Income and Collateral	<i>The information flows related to the triggering of a buy-in are currently discussed between professional associations.</i>	Open
B4	Cost	How will the participants be able to pass on the cost of the buy-in, if there is no business relationship in place?	GLF CSDR	This point will be part of the work undertaken by the professional associations.	Open
Internalised settlement					

5.4 Bibliography

5.4.1 General Documentation

- a. Regulation (EU) no. 909/2014 (namely CSDR Regulation): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32014R0909&from=EN>
- b. ESMA Q&A: https://www.esma.europa.eu/sites/default/files/library/esma70-708036281-2_csd_r_gas.pdf

5.4.2 CSD/ICSD license

- a. Delegated Regulation (EU) no. 2017/390 (namely RTS on prudential requirements for CSDs): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32017R0390&from=EN>
- b. Delegated Regulation (EU) no. 2017/392 (namely RTS on CSD requirements): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32017R0392&from=EN>
- c. Implementing Regulation (EU) no. 2017/394 (namely ITS on CSD requirements): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32017R0394&from=EN>
- d. ESMA Briefing note on LEI – October 9th 2017: https://www.esma.europa.eu/sites/default/files/library/esma70-145-238_lei_briefing_note.pdf

5.4.3 Internalised settlement

- a. Delegated Regulation (EU) no. 2017/391 (namely RTS on internalised settlement): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32017R0391&from=EN>
- b. Implementing Regulation (EU) no. 2017/393 (namely ITS on internalised settlement): <http://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32017R0393&from=EN>
- c. ESMA guidelines: https://www.esma.europa.eu/sites/default/files/library/esma70-151-1258_final_report_-_csdr_guidelines_on_internalised_settlement_reporting.pdf

5.4.4 Fail and buy-in-related penalties

- a. Delegated Regulation (EU) no. 2017/389 (defines calculation formulas and rates)
- b. Delegated Regulation (EU) no 2018/1229

5.5 Regulatory references on fail-related penalty processing

5.5.1 Main definitions

CSDR (article 2)

7) "Settlement" means the completion of a securities transaction where it is concluded with the aim of discharging the obligations of the parties to that transaction through the transfer of cash or securities, or both;

9) "Transfer order" means transfer order as defined in the second indent of point (i) of Article 2 of Directive 98/26/EC;

15) "Settlement fail" means the non-occurrence of settlement, or partial settlement of a securities transaction on the intended settlement date, due to a lack of securities or cash and regardless of the underlying cause;

2018/1229 (article 1)

(e) 'Settlement instruction' means a transfer order as defined in point (i) of Article 2 of Directive 98/26/EC of the European Parliament and of the Council

98/26/EC (article 2)

i) "Transfer order":

- any instruction by a participant to place at the disposal of a recipient an amount of money by means of a book entry on the accounts of a credit institution, a central bank or a settlement agent, or any instruction which results in the assumption or discharge of a payment obligation as defined by the rules of the system, or

- an instruction by a participant to transfer the title to, or interest in, a security or securities by means of a book entry on a register, or otherwise;

5.5.2 Scope of Financial Instruments concerned

CSDR – Article 5 Intended settlement date

1. Any participant in a securities settlement system that settles in that system on its own account or on behalf of a third party transactions in transferable securities, money-market instruments, units in collective investment undertakings and emission allowances shall settle such transactions on the intended settlement date.

CSDR – Article 7 Measures to address settlement fails

10. Paragraphs 2 to 9 shall apply to all transactions of the financial instruments referred to in Article 5(1) which are admitted to trading or traded on a trading venue or cleared by a CCP as follows:

a) for transactions cleared by a CCP, the CCP shall be the entity that executes the buy-in according to paragraphs 3 to 8;

b) for transactions not cleared by a CCP but executed on a trading venue, the trading venue shall include in its internal rules an obligation for its members and its participants to apply the measures referred to in paragraphs 3 to 8;

c) for all transactions other than those referred to in points (a) and (b) of this sub-paragraph, CSDs shall include in their internal rules an obligation for their participants to be subject to the measures referred to in paragraphs 3 to 8.

Q&A of the European Commission

16. What is the scope of the settlement discipline measures referred to in Article 7(2) to (9) as regards the financial instruments covered?

Article 7(10) provides that the settlement discipline measures referred to in Article 7(2) to (9) apply to financial instruments referred to in Article 5(1) (i.e. transferable securities, money-market instruments, units in collective investment undertakings and emission allowances) that are:

a) admitted to trading on trading venues (OTC transactions); or

b) traded on a trading venues (non-OTC transactions); or

c) cleared by a CCP (OTC and non-OTC transactions regardless of whether the financial instruments are or not admitted to trading on trading venues)

Article 7(10) therefore excludes from the scope of application of Article 7(2) to (9), transactions in financial instruments that are not admitted to trading and not cleared by a CCP.

5.5.3 Scope of instructions

5.5.3.1 General framework

CSDR – Article 7 Measures to address settlement fails

2. For each securities settlement system it operates, a CSD shall establish procedures that facilitate settlement of transactions in financial instruments referred to in Article 5(1) that are not settled on the intended settlement date. These procedures shall provide for a penalty mechanism which will serve as an effective deterrent for participants that cause settlement fails.

5.5.3.2 "Matched" status

2018/1229 – Article 5 Matching and population of settlement instructions

2.CSDs shall require participants to match their settlement instructions through the functionality referred to in paragraph 1 prior to their settlement, except in the following circumstances:

- (a) where the CSD has accepted that the settlement instructions have already been matched by trading venues, CCPs or other entities;
- (b) where the CSD itself has matched the settlement instructions;
- (c) in the case of free of payment ('FoP') settlement instructions, referred to in point (g)(i) of Article 13(1), which consist of orders for transfers of financial instruments between different accounts opened in the name of the same participant or managed by the same account operator.

Account operators referred to in point (c) shall include entities that have a contractual relationship with a CSD and that operate securities accounts maintained by that CSD by means of recording book entries into those securities accounts.

2018/1229 – Article 16 Calculation and application of cash penalties

Where matching is required pursuant to Article 5(2), cash penalties shall only be applied to matched settlement instructions.

5.5.3.3 'On hold' instructions

Article 16 Calculation and application of cash penalties

CSDs for each settlement instruction that fails to settle. The calculation referred to in the first subparagraph shall include settlement instructions that have been put on hold by a participant.

5.5.3.4 Late instructions

Article 16 Calculation and application of cash penalties

3. Where a settlement instruction has been entered into the securities settlement system or has been matched after the intended settlement date, cash penalties shall be calculated and applied as from the intended settlement date. Where new settlement instructions are entered into the securities settlement system for any non-delivered financial instruments in accordance with Article 27(10), Article 29(11) or Article 31(11), cash penalties shall apply to the new settlement instructions from the day those instructions are entered into the securities settlement system. Where settlement instructions have been matched after the intended settlement date, cash penalties for the period between the intended settlement date and the business day prior to the day on which matching has taken place shall be paid by the last participant who has entered or modified the relevant settlement instruction in the securities settlement system.

4. CSDs shall provide each relevant participant with the details of the calculation of the penalties for each failed settlement instruction on a daily basis, including details on the account to which each failed settlement instruction refers.

5.5.4 Calculation of penalties

5.5.4.1 Level and method of penalty application

CSDR – Article 7 Measures to address settlement fails

The penalty mechanism referred to in the first sub-paragraph shall include cash penalties for participants that cause settlement fails ('failing participants'). Cash penalties shall be calculated on a daily basis for each business day that a transaction fails to be settled after its intended settlement date until the end of a buy-in process referred to in paragraph 3, but no longer than the actual settlement day. The cash penalties shall not be configured as a revenue source for the CSD.

2018/1229 – Article 16 Calculation and application of cash penalties

1. The cash penalties referred to in Article 7(2) of Regulation (EU) No 909/2014 shall be calculated and applied by CSDs for each settlement instruction that fails to settle. The calculation referred to in the first subparagraph shall include settlement instructions that have been put on hold by a participant.

(...)

2. Cash penalties shall be calculated and applied at the end of each business day where the settlement instruction fails to settle.

5.5.4.2 Calculation formulae

The delegated regulation 2017/389 gives the rates applicable according to the type of financial instrument and specifies in article 2 that the reference price is always used, therefore even in case of a fail due to lack of cash (this is the chosen rate which varies).

2017/389 – Recital (4)

... Cash penalties should be therefore the result of multiplying the number of financial instruments underlying the transaction that failed to settle by the relevant reference price. The establishment of reference prices should be based on objective and reliable data and methodologies.

2017/389 – Article 2 Calculation of cash penalties

The level of cash penalties referred to in the third sub-paragraph of Article 7(2) of Regulation (EU) No 909/2014 for settlement fails of transactions in a given financial instrument shall be calculated by applying the relevant penalty rate set out in the Annex to this Regulation to the reference price of the transaction determined in accordance with Article 3 of this Regulation.

2017/389 – Article 3 Reference price of the transaction

2. The reference price referred to in paragraph 1 shall be used to calculate the level of cash penalties for all settlement fails, irrespective of whether the settlement fail is due to a lack of securities or cash.

ESMA Q&A

Settlement Discipline Questions 1 – Matching settlement instructions

How often should the exchange rate used to determine the tolerance level for settlement instructions in other currencies than EUR (referred to in Article 6 of the RTS on Settlement Discipline) be updated?

Settlement Discipline Answers 1

ESMA considers that the exchange rate should be updated annually. To ensure consistency across CSDs, CSDs should use the same exchange rates. Therefore, CSDs should use the official exchange rates of the ECB, where available, valid on 1 January of the respective calendar year.

Settlement Discipline Questions 2 – Cash penalties: joint penalty mechanism

(a) When CSDs use a common settlement infrastructure, which part of the penalty mechanism should be jointly managed? Can such CSDs use multiple service providers to operate the penalty mechanism?

(b) Is the use of a common framework or rulebook sufficient in order to satisfy the requirement for a joint establishment and joint management of the cash penalty mechanism under Article 20 of the RTS on Settlement Discipline?

Settlement Discipline Answers 2

(a) According to Article 20 of the RTS on Settlement Discipline, when CSDs use a common settlement infrastructure, the entire penalty mechanism should be jointly managed. It is thus expected that the calculation, application, collection and redistribution of cash penalties is jointly managed.

If multiple service providers are used, it is up to the CSDs using a common settlement infrastructure to prove how they can ensure the joint management of the penalty mechanism, in particular with regard to the coordination and exchange of information between the different service providers.

(b) No. Such a framework may be helpful in terms of ensuring an increased degree of harmonisation across all CSDs in the EU, however, in order to ensure compliance with Article 20 of the RTS on settlement discipline, in the case of CSDs that use a common settlement infrastructure, the penalty mechanism should be jointly established, managed and operated by the respective CSDs. This should include at least:

- i. the joint governance and legal enforceability of common rules and procedures related to the application of the penalty mechanism;*
- ii. the use of common reference data and prices;*
- iii. the use of a single calculation engine, which does not require reconciliation operations amongst the involved CSDs related to the application of the penalty mechanism.*

Settlement Discipline Questions 3 – Cash penalties: calculation

(a) Is bilateral netting followed by aggregation of the amounts resulting in one credit and one debit amount per CSD participant in line with Article 17 of the RTS on settlement discipline?

(b) Which rate should be applied (the securities rate or the cash rate) for the calculation of cash penalties in accordance with Article 7(2) of CSDR and Articles 2 and 3 of the Commission Delegated Regulation (EU) 2017/389?

(c) Should cash penalties be applied to settlement fails in the case of receive free of payment ('RFP') settlement instructions, receive with payment ('RWP') settlement instructions, or crediting payment free of delivery ('CPFOD') settlement instructions (as referred to in Article 13(1)(g) of the RTS on Settlement Discipline), which are put on hold?

(d) When should penalty rates for financial instruments traded on SME growth markets apply, as set out in the Annex to the Commission Delegated Regulation (EU) 2017/389?

(e) Should the net amounts of cash penalties referred to in Article 17 of the RTS on settlement discipline be calculated and communicated only in Euros to the CSD participants?

Settlement Discipline Answers 3

(a) Yes.

(b) The cash rate should be applied if the reason for the settlement fail is applicable to the leg of the transaction which delivers the cash, while the securities rate should be applied in case the reason for the fail is applicable to the leg of the transaction which delivers the securities.

(c) Yes. Regarding receive free of payment ('RFP') settlement instructions, receive with payment ('RWP') settlement instructions, or crediting payment free of delivery ('CPFOD') settlement instructions (as referred to in Article 13(1)(g) of the RTS on Settlement Discipline), which are put on hold, cash penalties should be applied in order to penalise the non-timely settlement and foster settlement discipline, even if the participant who put the instruction on hold did not suffer from the non-delivery of securities or cash.

(d) The penalty rates for SME growth market instruments should only apply if the particular trade has actually taken place on an SME growth market. In order for these penalty rates to apply, the same information identifying the relevant SME growth market should be included in the field related to the place of trading in both corresponding settlement instructions.

(e) No. The net amounts of cash penalties referred to in Article 17 of the RTS on Settlement Discipline should be calculated per settlement currency and should not be converted into Euros.

*Settlement Discipline Questions 4 – Cash penalties: scope *new**

(a) Are there exceptional situations where the cash penalty mechanism provided for under Article 7(2) of CSDR should not be applied?

Settlement Discipline Answers 4

(a) Yes. In addition to situations where insolvency proceedings are opened against the failing participant in accordance with Article 7(12) of CSDR, cash penalties should not be applied in the following situations where settlement cannot be performed for reasons that are independent from the involved participants:

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

ii. 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;

iii. 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;

iv. technical impossibilities at the CSD level that prevent settlement, such as: a failure of the infrastructure components, a cyber-attack, network problems.

CSDs should report the concrete cases falling in the above-mentioned categories to their competent authorities, and the competent authorities should have the possibility to ask the CSDs to apply cash penalties in the future in similar cases, if they consider the non-application of penalties unjustified.

5.5.5 Other regulatory requirements

5.5.5.1 Information

2018/1229 – Article 16 Calculation and application of cash penalties

4.CSDs shall provide each relevant participant with the details of the calculation of the penalties for each failed settlement instruction on a daily basis, including details on the account to which each failed settlement instruction refers.

5.5.5.2 Payment

2018/1229 - Article 17 Collection and distribution of cash penalties

1.CSDs shall charge and collect on at least a monthly basis the net amount of cash penalties to be paid by each failing participant. Cash penalties shall be deposited into a dedicated cash account.

2.CSDs shall distribute on at least a monthly basis the net amount of cash penalties referred to in paragraph 1 to receiving participants affected by settlement fails.

5.5.5.3 Particular case of CCPs

2018/1229 – Recital (22)

The penalty mechanism should apply to all failed transactions, including cleared transactions. Where the failing participant is a CCP, however, the penalty should not be due by that CCP, but by the relevant clearing member that caused the settlement fail. For that purpose, CSDs should provide CCPs with all the necessary information on the settlement fail and the calculation of the penalty to enable CCPs to charge a penalty to the relevant clearing member and to distribute the collected amount to the clearing member that suffered from the subsequent settlement fail on the same financial instruments.

2018/1229 – Article 19 Penalty mechanism where the participant is a CCP

Where the failing or the receiving participant is a CCP, CSDs shall ensure the following:

(a) that CCPs are provided with the calculation of the cash penalties for the failed settlement instructions submitted by those CCPs;

(b) that CCPs collect the cash penalties referred to in point (a) from the clearing members that caused the settlement fails;

(c) that CCPs distributes the cash penalties referred to in point (b) to the clearing members that are affected by the settlement fails;

(d) that CCPs report to the CSD on the penalties that they have collected and distributed, on a monthly basis.

5.5.5.4 Harmonisation between CSDs

T2S case

2017/1229 – Article 20 CSDs that use a common settlement infrastructure

CSDs that use a common settlement infrastructure, including where some of their services or activities have been outsourced as referred to in Article 30(5) of Regulation (EU) No 909/2014, shall jointly establish the penalty mechanism referred to in Article 7(2) of Regulation (EU) No 909/2014 and jointly manage the modalities for the calculation, application, collection and distribution of cash penalties in accordance with this Regulation.

5.5.6 Reference data

5.5.6.1 Financial instruments

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5.5.6.2 Reference prices

2017/389 – Article 3 Reference price of the transaction

1. The reference price referred to in Article 2 shall be equal to the aggregated market value of the financial instruments determined in accordance with Article 7 for each business day that the transaction fails to be settled.

2017/289 – Article 7 Determination of market values

The market value of financial instruments referred to in Articles 3, 5 and 6 of this Regulation shall be determined as follows:

- a) for financial instruments referred to in Article 3(1) of Regulation (EU) No 600/2014 admitted to trading on a trading venue within the Union, the market value of the relevant financial instrument shall be the closing price of the most relevant market in terms of liquidity referred to in Article 4(1)(a) of Regulation (EU) No 600/2014;
- b) for financial instruments admitted to trading on a trading venue within the Union other than those referred to in point (a), the market value shall be the closing price derived from the trading venue within the Union with the highest turnover;
- c) for financial instruments other than those referred to in points (a) and (b), the market value shall be determined on the basis of a predetermined methodology approved by the competent authority of the relevant CSD that refers to criteria related to reliable market data, such as market prices available across trading venues or investment firms.

2017/389 – Article 9 Entry into force and application

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

It shall apply from 10 March 2019

By way of derogation from the second paragraph, ...

- b) Article 7 shall apply from the date referred to in the second paragraph of Article 55 of Regulation (EU) No 600/2014; - Article 55 of MIFIR is the one which gives the date of entry into force and application of MIFIR, on January 3, 2018.

5.5.7 Operating costs

2018/1229 – Article 18 Costs of the penalty mechanism

1. CSDs shall not use cash penalties to cover costs related to the penalty mechanism.
2. CSDs shall disclose, in detail, the amount of the costs referred to in paragraph 1 to participants.
3. CSDs shall charge participants separately for the costs of the penalty mechanism. Those costs shall not be charged on the basis of gross penalties applied to each participant.

5.5.8 Reminder MiFIDII (Level 2)

2017/593 – Article 5 Use of client financial instruments

3. Member States shall ensure that investment firms take appropriate measures to prevent the unauthorised use of client financial instruments for their own account or the account of any other person such as:

(a) the conclusion of agreements with clients on measures to be taken by the investment firms in case the client does not have enough provision on its account on the settlement date, such as borrowing of the corresponding securities on behalf of the client or unwinding the position;

(b) the close monitoring by the investment firm of its projected ability to deliver on the settlement date and the putting in place of remedial measures if this cannot be done; and

(c) the close monitoring and prompt requesting of undelivered securities outstanding on the settlement day and beyond.

5.6 Regulatory references on internalised settlement processing

Article 2

1. The reports referred to in the first subparagraph of Article 9(1) of Regulation (EU) No 909/2014 shall include the following information:

(a) country code of the place of establishment of the settlement internaliser;

(b) reporting timestamp;

(c) period covered by the report;

(d) identifier of the settlement internaliser;

(e) contact details of the settlement internaliser;

(f) the aggregated volume and value, expressed in euros, of internalised settlement instructions settled by the settlement internaliser during the period covered by the report;

(g) the aggregated volume and value, expressed in euros, of internalised settlement instructions settled by the settlement internaliser during the period covered by the report, for each of the following types of financial instruments:

(i) transferable securities referred to in point (a) of Article 4(1)(44) of Directive 2014/65/EU of the European Parliament and of the Council;

(ii) sovereign debt referred to in point (61) of Article 4(1) of Directive 2014/65/EU;

(iii) transferable securities referred to in point (b) of Article 4(1)(44) of Directive 2014/65/EU, other than those referred to in point (ii) of point (g) of this subparagraph;

(iv) transferable securities referred to in point (c) of Article 4(1)(44) of Directive 2014/65/EU;

(v) exchange-traded funds as defined in point (46) of Article 4(1) of Directive 2014/65/EU;

(vi) units in collective investment undertakings, other than exchange-traded funds;

(vii) money-market instruments, other than those referred to in point (ii);

(viii) emission allowances;

(ix) other financial instruments.

(h) the aggregated volume and value, expressed in euros, of all internalised settlement instructions, for each of the following types of securities transactions settled by the settlement internaliser during the period covered by the report:

(i) purchase or sale of securities;

(ii) collateral management operations;

(iii) securities lending or securities borrowing;

(iv) repurchase transactions;

(v) other securities transactions.

(i) the aggregated volume and value, expressed in euros, of all internalised settlement instructions, settled by the settlement internaliser during the period covered by the report, covering the following types of clients:

(i) professional clients as defined in point (10) of Article 4(1) of Directive 2014/65/EU;

(ii) retail clients as defined in point (11) of Article 4(1) of Directive 2014/65/EU.

(j) the aggregated volume and value, expressed in euros, of all internalised settlement instructions referring to cash transfers settled by the settlement internaliser during the period covered by the report;

(k) the aggregated volume and value, expressed in euros, of all internalised settlement instructions settled by the settlement internaliser during the period covered by the report, per each CSD that provides the core service referred to in point 1 or 2 of Section A of the Annex to Regulation (EU) No 909/2014 in relation to the underlying securities;

(l) the aggregated volume and value, expressed in euros, of all internalised settlement instructions referred to in points (g) to (j), per each CSD that provides the core service referred to in point 1 or 2 of Section A of the Annex to Regulation (EU) No 909/2014 in relation to the underlying securities;

(m) the aggregated volume and value, expressed in euros, of failed internalized settlement instructions referred to in points (f) to (l) that fail to be settled as during the period covered by the report;

(n) the rates of internalised settlement instructions referred to in points (f) to (l) that fail to be settled as compared to the following:

(i) the aggregated value, expressed in euros, of internalised settlement instructions settled by the settlement internaliser and failed internalised settlement instructions;

(ii) the aggregated volume of internalised settlement instructions settled by the settlement internaliser and failed internalised settlement instructions.

For the purposes of points (k) and (l) of the first subparagraph, if the information on the CSD that provides the core service referred to in point 1 or 2 of Section A of the Annex to Regulation (EU) No 909/2014 in relation to the underlying securities issue is not available, the ISIN of the securities shall be used as a proxy, by splitting the data by the first two characters of the ISIN codes.

2. Where available, the exchange rate of the European Central Bank on the last day of the period covered by the reports shall be used for the conversion of other currencies into euros.

3. The aggregated value of internalised settlement instructions referred to in paragraph 1 shall be calculated as follows:

(a) in the case of internalised settlement instructions against payment, the settlement amount of the cash leg;

(b) in the case of internalised settlement instructions free of payment, the market value of the securities or, if not available, the nominal value of the securities.

The market value referred to in point (b) of the first subparagraph shall be calculated as follows:

(a) for financial instruments referred to in Article 3(1) of Regulation (EU) No 600/2014 of the European Parliament and of the Council⁶ admitted to trading on a trading venue within the Union, the value determined on the basis of the closing price of the most relevant market in terms of liquidity referred to in Article 4(6)(b) of that Regulation;

(b) for financial instruments admitted to trading on a trading venue within the Union other than those referred to in point (a), the value determined on the basis of the closing price of the trading venue within the Union with the highest turnover;

(c) for financial instruments other than those referred to in points (a) and (b) the value determined on the basis of a price calculated using a pre-determined methodology, approved by the competent authority, that refers to criteria related to market data, such as market prices available across trading venues or investment firms.

ANNEXE I

Modèle pour la notification et la transmission d'informations sur les règlements internalisés

Règlement internalisé									
Informations sur l'internalisateur de règlement									
		C0010							
Code du pays	R0010								
Horodatage de la notification	R0020								
Période de référence	R0030								
LEI	R0040								
Nom de la personne responsable	R0050								
Fonction de la personne responsable	R0060								
N° de téléphone	R0070								
Adresse de courrier électronique	R0080								
		Agrégat						Taux	
		Régulé		Défaut de règlement		Total		Défaut de règlement	
		Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume (%)	Valeur (%)
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090
Total général	R0090								
Instruments financiers									
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) a), de la directive 2014/65/UE du Parlement européen et du Conseil (1)	R0100								
Dette souveraine visée à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0110								
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) b), de la directive 2014/65/UE, autres que la dette souveraine visée à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0120								

		Agrégat						Taux	
		Régulé		Défaut de règlement		Total		Défaut de règlement	
		Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume (%)	Valeur (%)
		C0020	C0030	C0040	C0050	C0060	C0070	C0080	C0090
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) c), de la directive 2014/65/UE	R0130								
Fonds cotés au sens de l'article 4, paragraphe 1, point 46), de la directive 2014/65/UE	R0140								
Parts d'organismes de placement collectif autres que les fonds cotés	R0150								
Instruments du marché monétaire autres que la dette souveraine visée à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0160								
Quotas d'émission	R0170								
Autres instruments financiers	R0180								
Type de transactions									
Achat ou vente de titres	R0190								
Opérations de gestion de garanties (collatéral)	R0200								
Prêts de titres et emprunts de titres	R0210								
Opérations de pension	R0220								
Autres transactions sur titres	R0230								
Type de client									
Clients professionnels au sens de l'article 4, paragraphe 1, point 10), de la directive 2014/65/UE	R0240								
Clients de détail au sens de l'article 4, paragraphe 1, point 11), de la directive 2014/65/UE	R0250								
Transferts d'espèces									
Total des transferts d'espèces	R0260								

Informations sur chaque DCT émetteur									
		C0100							
Identifiant du DCT émetteur	R0270								
Code du pays du DCT émetteur	R0280								
		Agrégat					Taux		
		Régulé		Défaut de règlement		Total Régulé Défaut de règlement		Défaut de règlement	
		Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume (%)	Valeur (%)
		C0110	C0120	C0130	C0140	C0150	C0160	C0170	C0180
Total général	R0290								
Instruments financiers									
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) a), de la directive 2014/65/UE	R0300								
Dettes souveraines visées à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0310								
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) b), de la directive 2014/65/UE, autres que la dette souveraine visée à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0320								
Valeurs mobilières visées à l'article 4, paragraphe 1, point 44) c), de la directive 2014/65/UE	R0330								
Fonds cotés au sens de l'article 4, paragraphe 1, point 46), de la directive 2014/65/UE	R0340								
Parts d'organismes de placement collectif autres que les fonds cotés	R0350								
Instruments du marché monétaire autres que la dette souveraine visée à l'article 4, paragraphe 1, point 61), de la directive 2014/65/UE	R0360								
Quotas d'émission	R0370								
Autres instruments financiers	R0380								

		Agrégat						Taux	
		Régulé		Défaut de règlement		Total Régulé Défaut de règlement		Défaut de règlement	
		Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume	Valeur (EUR)	Volume (%)	Valeur (%)
		C0110	C0120	C0130	C0140	C0150	C0160	C0170	C0180
Type de transactions									
Achat ou vente de titres	R0390								
Opérations de gestion de garanties (collatéral)	R0400								
Prêts de titres et emprunts de titres	R0410								
Opérations de pension	R0420								
Autres transactions sur titres	R0430								
Type de client									
Clients professionnels au sens de l'article 4, paragraphe 1, point 10), de la directive 2014/65/UE	R0440								
Clients de détail au sens de l'article 4, paragraphe 1, point 11), de la directive 2014/65/UE	R0450								
Transferts d'espèces									
Total des transferts d'espèces	R0460								

(¹) Directive 2014/65/UE du Parlement européen et du Conseil du 15 mai 2014 concernant les marchés d'instruments financiers et modifiant la directive 2002/92/CE et la directive 2011/61/UE (JO L 173 du 12.6.2014, p. 349).



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