



*European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken*

EACB answer
to the CESR/ESCB consultation paper on the *“Draft recommendations for securities settlement systems and draft recommendations for central counterparties”*

23 January 2009

The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 28 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks’ business model. With 4.200 locally operating banks and 63.000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 160 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 50 million members and 750.000 employees and have a total average market share of about 20%.

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AN ASSOCIATION ON THE MOVE

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General remarks

The EACB appreciates the opportunity to send its remarks on the draft recommendations for securities settlement systems and for central counterparties that were elaborated by the European System of Central Banks (ESCB) and the Committee of European Securities Regulators (CESR).

Our members welcome that the issued recommendations are based on internationally agreed standards, e.g. the recommendations for central counterparties (CCPs) elaborated in 2004 by the Committee on Payment and Settlement Systems (CPSS) and by the International Organization of Securities Commissions (IOSCO).

Furthermore we very much appreciate that while central security depositories (CSDs) and CCPs are in scope of the ESCB-CESR recommendations, custodian banks are not. We consider this fact as reasonable since banks are already embedded in a harmonised regulatory framework including the Capital Requirement Directive and MiFID. For CCPs or CSDs a similar background is missing.

We took note that there is no reference to TARGET2-Securities (T2S) in the recommendations and would like to highlight that a reference to this project would certainly help to reach the goal of the recommendations. T2S could be the benchmark in terms of ensuring central bank money and delivery vs. payments settlement.

Taking into account that the recommendations are supposed to be the absolute minimum to be respected by a CSD or a CCP we would like to point out that in many cases national laws provide stricter requirements. If an infrastructure can provide cross-border services throughout Europe by compiling with these minimal obligations despite of stricter local laws, then these recommendations would reduce the level of soundness and safety as well as induce regulatory arbitrage. We therefore are against the concept of a "European passport".

Part 1: Draft Recommendations for Securities Settlement Systems

Recommendation 1 (pp. 17 – 21): Legal framework

- The term "interoperable system" is imprecise and should be defined more clearly in this section as well as in the glossary.

Recommendation 2 (pp. 22 – 24): Trade Confirmation and Settlement Matching

- Matching should also be recommended for FOP transactions, since FOP matching is an international best practice.
- Timely matching may be complicated in the absence of hold & release mechanisms; hence all CSDs should offer such mechanisms.

Recommendation 3 (pp. 25 – 27): Settlement Cycles and Operating Times

- Our members agree with the goal of harmonisation of settlement cycles, but would prefer a harmonisation on market level, rather than on the level of individual securities. For transaction executed over-the-counter markets should be allowed to negotiate freely their settlement cycles.



- We consider as important to harmonise solutions for managing fails on a European level. A buy-in regime is considered the optimal solution as the associated costs can be clearly allocated to specific transactions.

Recommendation 4 (pp. 28 – 30): Central Counterparties

- Also the possibility of servicing the market by an already existing CCP should be considered, when balancing the benefits and costs of establishing a CCP.

Recommendation 5 (pp. 31 – 34): Securities Lending

- We agree to aim to avoid and/or reduce settlement fails. But we disagree with a securities lending at the level of the CSD.
- In order to address possible competition concerns in the area of securities lending, we would advise that participants are offered a genuine possibility of also using other securities lending products.

Recommendation 8 (pp. 41 – 43): Settlement Finality

- Also for matched instructions a hold & release functionality would be appreciated by our members, in case there is no unilateral cancellation. However, for on-exchange / CCP transactions the respective rules should prevail.
- The approach outlined in C7 with respect to links to other settlement systems is welcomed by us. In addition it should also be a guiding principle for the design of CSD links under T2S.

Recommendation 10 (pp. 47 – 49): Cash Settlement Assets

- In case a CSD has any kind of remote access to a central bank (C3) we would like to point out that also other institutions should be granted the same possibility for competitive reasons.

Recommendation 11 (pp. 50 – 55): Operational risk

- In addition to the outlines also clearly defined rules for the allocation of costs in case of operational losses need to be considered for this recommendation.

Recommendation 12 (pp. 56 – 60): Protection of Customers' Securities

- As already mentioned in the general remarks above, we appreciate that custodian banks are out of scope of the recommendations: this part on protection of customers' securities should clearly be valid only for CSDs.
- Furthermore the concept of "investor CSD" used in this section is confusing. We would suggest deleting this term since an "investor CSD" in fact acts as global custodian in case it accesses to the issuer CSD but it is not able to fulfil a specific infrastructure role in ensuring the integrity of the issue.

Recommendation 14 (pp. 63 – 65): Access

- For us it is important that the same access criteria apply to all entities in the business on an equal basis.
- Also the actual process for reviewing memberships or account opening should be non-discriminatory and transparent.



- The sense of the sentence “Some CSDs may establish more stringent criteria for members that act as a custodian” is unclear. It would probably make sense to delete it.

Recommendation 15 (p. 66): Efficiency

- Also subsidiaries of CSDs located outside the EU should also apply to these rules if they are part of a group located in or having material business in the EU.

Recommendation 16 (pp. (67 – 69): Communication procedures, measuring standards and Straight-Through Processing (STP)

- The employment of translation or conversion mechanisms is only acceptable for us if it is made sure that users can access them without discrimination or additional costs. It is very important that CSDs are SWIFT compliant but allow the use of alternative communication mechanisms such as file transfer.

Recommendation 17 (pp. 70 – 71): Transparency

- It does make sense to provide not only balance sheet data to the market participants, but also a profit and loss account. In case of CSD groups operating in different markets the information should be provided for each market.

Recommendation 19 (pp. 75 – 78): Risks in Cross-System Links or Interoperable Systems

- This recommendation is not clear to us. Therefore we would appreciate a redrafted version of it.

Part 2: Draft Recommendations for Central Counterparties

Recommendation 1 (pp. 80 – 84): Legal risk

- It is not clear to whom this recommendation applies: a clear definition of what a CCP is – opposed to other institutions – is missing. The designation under the settlement finality directive could be a criterion to define the scope of the recommendations.
- We would suggest choosing the term “applicable law” rather than “chosen law”. This would ensure consistency with the European legal background.

Recommendation 2 (pp. 85 – 87): Participation Requirements

- The rules and their application by the CCP must be available in written form. Where the CCP engages in risk rating, the criteria should be available to the potential participant explaining the reason and consequences of a certain risk rating.
- The participants requirements should not rule out the CCP being responsible for gross misconduct and its rules and regulations should be in line with internal best practices as the SWIFT handbook.
- For us it is important that CCPs should treat participant’s data confidential and comply with European data protection rules. They should also inform about the location of their operations and in which jurisdiction client data is held.



Recommendation 3 (pp. 88 – 89): Measurement and management of credit exposures

- In case a CCP clears multiple trading venues, members who are using the CCP only for one market should not be exposed to losses of trading venues.

Recommendation 4 (pp. 90 – 92): Margin Requirements

- We would appreciate more clear outlines on the definition of “highly liquid instruments” in relation to this recommendation.

Recommendation 5 (pp. 93 – 97): Other Risk Controls

- It is very important for our members that the regulatory requirements for CCPs and their participants are well aligned. The rules governing the CCP should allow the clearing members to comply with provisions that regulate their relationship to their customers. A collateral pledge should therefore only comprise proprietary assets of the clearing member but no assets that belong to its customers.
- Also scenarios where the simultaneous crystallisation of different risks could occur should be taken into consideration.

Recommendation 6 (pp. 98 – 101): Default Procedures

- We would like to point out that the triggers of a default event should be clearly defined in paragraph C3.
- We consider point IV in C9 as not adequate with the role of a CCP.

Recommendation 7 (pp. 102 – 104): Custody and Investment Risks

- An institution providing custody services to the CCP should have Chinese walls in place. This should be mentioned in paragraph C2. Those would protect these functions and the information gained through these from its brokerage activities.
- The outlines in C2 allow CCPs to have a CSD or a custodian non-incorporated in the European Union. In order to limit systemic risks CSDs should be used by CCPs for settlement and collateral management and the recourse to custodians should not be admitted. In case a CCP has a custodian, it should be incorporated in the EU for ensuring an efficient supervision in Europe.
- We furthermore do not understand why investments in physical assets (e.g. computers, buildings,...) are not subject to the recommendation (C3). In addition we would appreciate to see investments in illiquid or volatile instruments prohibited.

Recommendation 10 (pp. 115 – 118): Physical Delivery

- We would suggest adding the case where the delivery cannot be carried out due to lack of securities. The consequence would usually be a buy-in with cash compensation.

Recommendation 11 (pp. 119 – 123): Risks in Links between CCPs

- Besides the harmonisation of operating hours based on target days and operating times, also daily schedules should be harmonised to avoid risks related to situations where assets are transferred from one CCP to another.



Recommendation 14 (pp. 129 – 130): Transparency

- We totally agree that transparency is of importance for the participants. However, we would appreciate a broader application of it in the actual text of this recommendation. Market participants should know what to expect in the case of turbulences and should not have to deal with different approaches if they are using more than one CCP. The recent financial crisis has shown how important it is to have internationally consistent and transparent rules and procedures in place.

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