

Securities settlement in the EU and central securities depositories (CSDs)

2012/0029(COD) - 07/03/2012 - Legislative proposal

PURPOSE: to make the European securities market safer and more efficient within the Union, which calls for coordinated EU action on Central Securities Depositories (CSDs).

PROPOSED ACT: Regulation of the European Parliament and of the Council.

BACKGROUND: the Central Securities Depositories (CSDs) are systemically important institutions for the financial markets. Any trade of securities on or off a securities exchange is followed by post-trade processes that lead to the settlement of that trade, which is the delivery of securities against cash. They play a **crucial role for the collateral market** especially for monetary policy purposes

While generally safe and efficient within national borders, CSDs combine and communicate less safely across borders, which means that an investor faces higher risks and costs when making a cross-border investment. For example, the number of settlement fails is higher for cross-border transactions than for domestic transactions and cross-border settlement costs are

up to four times higher than domestic settlement costs. These safety problems are the result of a number of factors, including:

- the length of the settlement cycle: the time between trade and settlement is not harmonised in the EU, creating disruptions when securities are settled cross-border;
- a small but substantial proportion of securities still exist in paper form: these are settled after a much longer settlement cycle, which increases the risk incurred by investors;
- settlement fails, which are situations where a transaction fails to be settled on the intended settlement date, are not subject to deterrent penalties in all markets and where they exist settlement discipline measures differ widely between markets;
- while Directive 98/26/EC on settlement finality in payment and securities settlement systems (SFD) reduces the disruption to a securities settlement system caused by insolvency proceedings against a participant in that system, it does not address other risks of the system or the resilience of the CSD operating the system.

The absence of an efficient single internal market for settlement also raises important concerns. Important barriers to the European post trading market continue to exist, such as for instance the limitation of securities issuers' access to CSDs, different national licensing regimes and rules for CSDs across the EU and limited competition between different national CSDs.

These barriers result in a very **fragmented market**. As a consequence, the cross-border settlement of transactions relies on unnecessarily complex holding 'chains' often involving several CSDs and several other intermediaries. This has a negative impact on the efficiency, but also on the risks associated with cross-border transactions.

IMPACT ASSESSMENT: the Commission conducted an impact assessment of policy alternatives. Policy options were assessed against the key objectives of increasing the safety, efficiency and level playing field for CSD services in Europe. The assessment was done by considering the effectiveness of achieving the objectives above and the cost efficiency of implementing different policy options.

LEGAL BASIS: Article 114 of the Treaty on the Functioning of the European Union (TFEU).

CONTENT: the proposal aims principally at **addressing the lack of safety and efficiency of securities settlement** and the resulting obstacles to the functioning of the internal market resulting from the divergent national rules regulating securities settlement and the activities of the CSDs, which operate securities settlement systems, by:

- introducing an **obligation to represent all transferable securities in book entry form and to record these** in CSDs before trading them on regulated venues;
- harmonising **settlement periods** and settlement discipline regimes across the EU;
- introducing a **common set of rules** inspired by international standards addressing the risks of the CSDs' operations and services.

As CSDs will be subject to identical substantive rules across the EU, they will benefit from uniform requirements for licensing and an EU wide **passport**, which will help remove the existing barriers of access.

As regards authorisation and supervision of CSDs, the proposed Regulation aims at striking a balance between the competences of national authorities and the interests of other competent authorities. The European Securities and Markets Authority (ESMA) will play a key role in resolving disputes, facilitating the cooperation arrangements between national authorities and developing technical standards in close consultation with the members of European System of Central Banks (ESCB).

Certain issues are already covered by existing Union legislation. For instance, securities settlement systems are already defined by Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2004/39/EC (MiFID) provides for certain rules of access by market participants to the securities settlement system of their choice. The proposed Regulation is consistent with these Union texts.

BUDGETARY IMPLICATIONS: this proposal has implications for the European Union budget related to the tasks allocated to ESMA. Estimated impact on the expenditure is EUR 1 093 million for the period 2013-2015.

The proposal also provides for a **co-financing** by the Member States to the amount of EUR 1 639 million over the 2013-2015 period.

DELEGATED ACTS: the Commission should be empowered to adopt delegated acts in accordance with Article 290 of the Treaty on the Functioning of the European Union (TFEU).