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

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OPINION OF THE EUROPEAN CENTRAL BANK on a proposal for a regulation on improving securities settlement in the European Union and on central securities depositories.

Together with Directive 2004/39/EC and the proposal for a regulation on OTC derivatives, central counterparties and trade repositories, this regulation will be part of the regulatory framework for market infrastructures and trading venues. The ECB **strongly supports the Commission's proposal** to strengthen the legal framework applicable to central securities depositories (CSDs) and to harmonise the rules underpinning the operation, authorisation and supervision of CSDs, as well as those relating to the issuance, holding and transfer of securities through such CSDs in the Union. It recommends that the regulation, and the corresponding implementing acts, be adopted prior to the launch of TARGET2-Securities (T2S) planned for June 2015.

The ECB makes the following recommendations on the proposal:

Scope of the regulation: the ECB notes that the **proposed regulation does not define 'financial instruments'** and that some parts of it apply only to 'securities' or transferable securities, whereas others also apply to money market instruments, units in collective investment undertakings and emission allowances. It is of the view that **all three core services should be regulated**.

The ECB recommends **further clarifying the scope of the proposed regulation**, both as regards the type of instruments it applies to and the definition of CSD, which should be amended to avoid regulatory arbitrage stemming from the creation by a CSD of two or three legal entities to perform different core activities without being subject to the Regulation applicable to CSDs. The ECB considers that each legal person offering any of the three core services indicated in Section A of the Annex should be subject to the Regulation.

Cooperation between authorities: the Regulation should ensure that:

- the powers of competent authorities and the European Securities and Markets Authority (ESMA) are complemented and balanced by an adequate involvement of the members of the ESCB;
- be consistent with the CPSS-IOSCO principles. An effective and close cooperation should be fostered between competent authorities and the members of the ESCB, both from an oversight perspective and as central banks of issue and without prejudice to central bank powers;
- facilitate comprehensive supervision and oversight in a cross-border context given the expected development of cross-border operations and settlement, as well as links between CSDs, a feature which will be facilitated and even fostered by the launch of the T2S common platform. Competent authorities should have the option of deciding on the appropriate form of cooperation arrangements, and the option of establishing colleges of authorities could be envisaged.

CSDs and banking type of ancillary services: the ECB makes the following points:

- the proposal distinguishes between banking type of ancillary services for the participants of a securities settlement system related to settlement service on the one hand, and banking type of ancillary services related to other core or ancillary services on the other hand. The ECB is of the view that the **distinction is not clear** and that the banking type of ancillary services referred to should be aligned as much as possible to the terminology in European banking legislation;

- the framework for the provision of ancillary banking services should be guided by an appropriate mitigation of risks whilst safeguarding the efficiency of CSDs in providing their services. Given the crucial nature of this issue, a **more comprehensive assessment of the various options for the provision of ancillary banking services** may be warranted. The ECB is prepared to contribute to such an assessment;
- there should be **no uncertainty** as to the exact scope of the ancillary banking services which designated credit institutions would be authorised to perform, the prudential requirements to which they would be subject, and their degree of autonomy vis-à-vis the banking legislative framework;
- the proposal limits the services to be provided by a designated credit institution that belongs to the same group as the CSD. The ECB recommends **extending this limitation to all credit institutions providing banking services listed in Section C of the Annex** for the participants of a securities settlement system having regard to the potential adverse effects on the ability of the CSD to continue to perform its functions, in particular those based on a delivery versus payment mechanism, in the case of a resolution or insolvency of the credit institution;
- the ECB considers that the procedure for granting a derogation is rather complex and could be streamlined to achieve the necessary degree of certainty and uniformity.

Consistency with global standards for CSDs: there are some inconsistencies between the CPSS-IOSCO principles and the proposed regulation, which the ECB recommends addressing: (i) requirements for tiered participation are not addressed; (ii) the need to manage risks stemming from interdependencies is mentioned only in the context of operational risk; (iii) the proposal regulation does not distinguish between deferred net settlement systems (DNS) that provide a settlement guarantee and those DNS that do not.

Conflict of laws: noting that the proposal provides as a general rule that any question with respect to proprietary aspects in relation to securities held by a CSD is governed by the law of the country where the securities account is maintained, the ECB strongly objects to the introduction of the additional conflict of laws rules which would be inconsistent with existing Union legislation and would affect legal certainty.

Furthermore, the ECB considers it necessary to **harmonise the various Union legal frameworks for holding and disposing of securities** and the exercise of rights attached to securities in line with the final report of the Legal Certainty Group.

Specific regime for resolution of CSDs: the ECB recommends adopting a specific, comprehensive regime for the resolution of CSDs.