Briefing note

September 2014

EU adopts new rules for CSDs

On 28 August the Regulation on Central Securities Depositories (CSDs) was published in the Official Journal. The Regulation aims to harmonise the authorisation and supervision of CSDs across the EU and to improve settlement discipline in the securities settlement systems (SSSs) that CSDs operate. The Regulation comes into force on 17 September 2014 and its various provisions will begin to apply at different points from January 2015. The Regulation is directly applicable in Member States though Level 2 measures are required to implement a number of its provisions.

In terms of post-crisis reform of financial market infrastructure, the Regulation can be seen as the settlement world's adjunct to EMIR (for clearing) and MiFID 2 (for trading). However, the Regulation's origins pre-date the financial crisis considerably. Stretching back over a decade or more, various studies have demonstrated the high post-trade costs associated with securities dealing in the EU. Most famously, the first and second Giovannini Group reports from 2001 and 2003 identified a range of barriers to post-trade efficiency. Historically, securities clearing and settlement systems in the EU have developed nationally. Domestic monopolies functioning under uniform technical, regulatory and legal frameworks have tended to predominate. Consequently, the EU cross-border settlement landscape has been characterised by higher cost and complexity (and sometimes weaker security) than in other important markets such as the United States.

The Regulation should be seen against this background, and as an attempt to address some of the weaknesses inherent in a post-trade landscape that has fragmented along national lines. On paper at least the Regulation makes an important contribution towards establishing a more efficient and competitive environment for EU securities settlement. However, the Regulation does nothing to solve conflicts of laws questions that inevitably arise in securities holdings across international borders and also creates the potential for yet more complex cross-border holding patterns. Despite the aspirations underpinning the Regulation, the more fundamental impediments to the EU enjoying the sort of low cost settlement landscape that characterises the US (chiefly the lack of a single European property and contract law) remain and will continue to do so for the foreseeable future. Furthermore, within the pages of the Regulation potentially lurk an array of compliance costs and complexities that could offset some of the anticipated benefits for participants in EU financial markets.

Apart from CSDs themselves, the banks providing access to SSS via their custody and settlement businesses are most likely to be affected by the Regulation. However, the brokers that act as the clients of those banks and who hold CCP and exchange memberships will also experience a direct impact, particularly from the Regulation's settlement discipline regime.

CSD Regulation – key features

- Full immobilization / dematerialization of EU issued securities
- Mandatory T+2 settlement date for most venue executed transactions
- Measures to prevent settlement failure
- Settlement discipline including cash penalties for system participants who cause settlement failure
- Compulsory buy-in process if settlement failure lasts more than 4 days
- Requirement for CSDs to obtain authorisation from national regulator
- Controls on CSDs outsourcing key functions
- Passport to permit authorized CSDs to provide services in other member states
- Obligation for CSD participants to offer individual client segregation

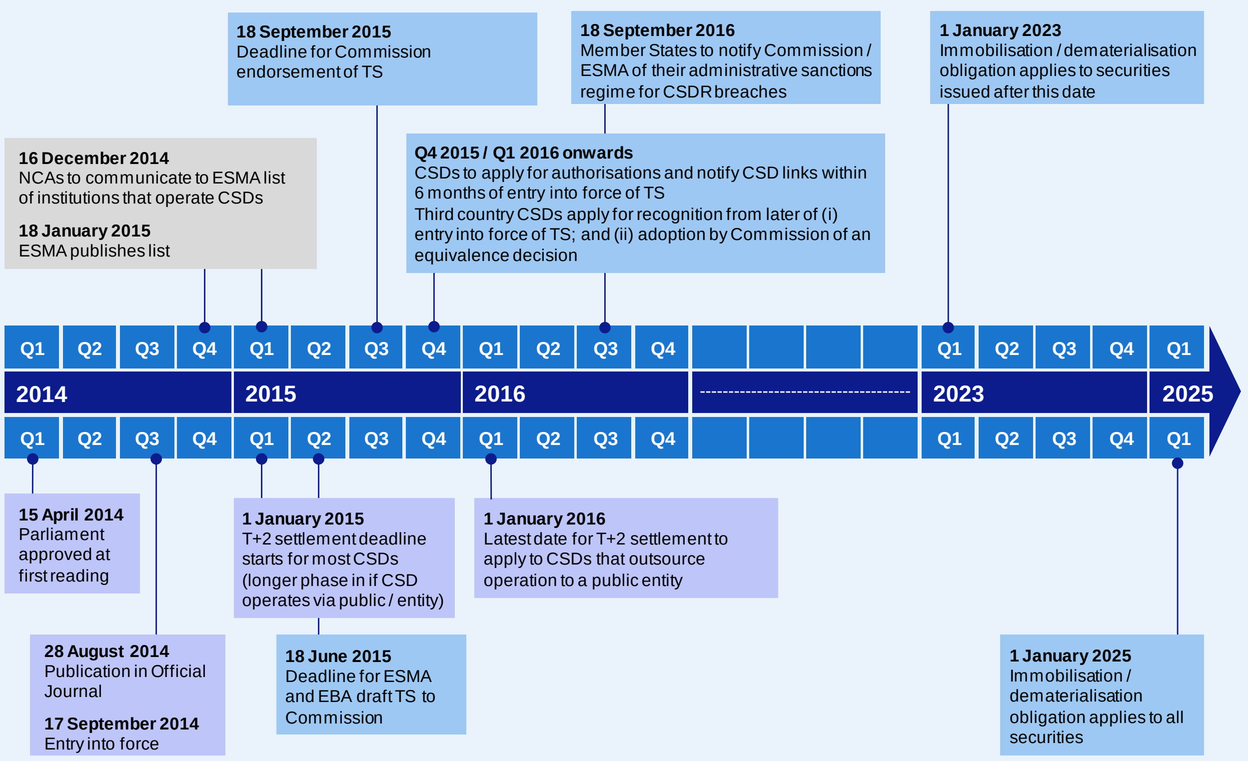
- Third country CSDs recognised by ESMA may operate within the EU
- Organisational requirements for CSDs (governance, management arrangements etc.)
- Conduct of business requirements for CSDs (including non-discriminatory access to SSS)
- CSD services requirements to promote integrity of securities issuance and manage safekeeping risks for participants and their clients
- Prudential rules for CSDs
- Risk controls on links between CSDs
- Freedom for issuers to record their securities in any EU CSD
- Controls on provision by CSDs of settlement overdrafts and related banking services ancillary to settlement

Timing of implementation

In some cases, the timing of implementation is clearly articulated in the Regulation but in other cases activation of new rules is linked to finalization of Level 2 measures, leading to some uncertainties in the timetable. The obligation to record securities in book entry form applies from 1 January 2023 for securities issued after that date and from 1 January 2025 for all others. The T+2 obligation applies from 1 January 2015 (or, where the relevant venue has access to a CSD that has outsourced settlement to a public entity, at least six months prior to the outsourcing, and in any event from 1 January 2016).

The settlement discipline regime will begin to apply from the date that relevant Commission implemented measures enter into force – likely to be some time in late 2015 or early 2016. Unhelpfully, the Regulation does not explicitly state when various other obligations imposed on CSDs will apply though it seems mostly likely that they cannot apply until the CSDs themselves have become authorized pursuant to the new national authorization process (this is similar to the linking of Article 39 and other "CCP obligations" under EMIR to the central counterparty (CCP) authorization process).

CSDR: illustrative implementation timeline



T+2 Securities Settlement

Perhaps the most important change heralded by the Regulation is the requirement for all EU securities transactions executed on a venue (i.e. a regulated market (RM), multilateral trading facility (MTF) or organised trading facility (OTF)) to settle on a T+2 timetable. There is a carve-out for transactions that are bilaterally negotiated but executed on venue and for transactions executed bilaterally but reported to a venue. The speedier T+2 settlement process should reduce the tenor of any settlement related counterparty credit risk, potentially releasing capital for faster reinvestment and possibly easing liquidity pressure during periods of high volatility.

Whilst the drafting of the relevant provisions in the Regulation is rather unclear, it appears that the regulatory obligation to ensure T+2 settlement primarily falls on participants in the relevant SSS. (In many cases these participants will simply be the agents of the buyer and seller and are unlikely to be transaction counterparties themselves). Breaking down the opaque drafting, the Regulation provides that: *(a) "[SSS] participants" shall settle transactions on the "intended settlement date"; (b) subject to exceptions, that date shall be no later than T+2; and (c) ensuring that the T+2 requirement is satisfied is the responsibility of the regulator which supervises the relevant trading venue.* It is perhaps strange that the legislator has not explicitly imposed any responsibility for T+2 settlement on the principal transaction counterparties whose failure (or whose clients' failure) to pay or deliver would be the most likely cause of a settlement failure in practice.

The exact scope of the "bilateral negotiation" exception is unclear. While it is obviously helpful for transactions that are completely "off venue" (i.e. genuine OTC transactions), there is less clarity as to whether or not it would apply to trades that are executed on organized markets which are quote-driven rather than based around a central order book (fixed income MTFs for example).

Many fixed income transactions are executed outside formal trading venues. For these OTC transactions parties will remain free to set their own settlement date. However, the T2S Steering Group on T+2 has suggested that the T+2 settlement period should extend as widely as possible and that for OTC Eurobond transactions, the presumption should be for T+2 settlement, unless both parties to the trade agree otherwise (and the International Capital Market Association is changing its standard settlement cycle in line with this recommendation).

Settlement discipline

The Regulation's settlement discipline measures impose obligations on trading venues, investment firms and CSDs. First, trading venues are required to establish procedures that enable confirmation of trade details on the date of execution. Secondly, firms themselves are required to put in place measures to limit settlement fails (to consist at least of arrangements ensuring the prompt communication prior to the settlement date of securities allocation and other trade terms between firms and their professional clients). Thirdly, CSDs are required to establish incentives to encourage timely settlement on the SSS that they operate. Acting in cooperation with the European System of Central Banks, ESMA is required to develop technical standards that will delineate more precisely the arrangements that firms and CSDs will need to put in place.

Settlement failure

In addition to measures designed to reduce the likelihood of settlement failure, the Regulation also mandates processes to remedy failed settlements and requires CSDs to monitor settlement failures on the SSS that they operate, providing regular reports to regulators. Notably, CSDs are required to impose cash penalties on participants that cause settlement fails. These penalties, intended to deter settlement failure, will apply daily for every day that a transaction fails to settle after the intended settlement date. The Regulation prevents CSDs from configuring penalties as a source of revenue. In many cases, settlement failure is unlikely to be to be the fault of the CSD participants but rather more likely to be caused by the default of participants' clients. In practice, therefore, CSD participants who are penalised under the new settlement failure regime may potentially seek to push the costs of such penalties down the transaction chain to their clients where they consider the failure to be the client's fault.

If a failure continues for an "extension period" of more than four days after the intended settlement date, then unless the participants bilaterally cancel the transaction, the Regulation requires a buy-in process to effect the settlement. A longer extension period of up to 7 days may apply if the shorter period would affect the smooth functioning of the relevant market. However, for centrally cleared cash equities transactions, the shorter

4 day period will always apply. If the buy-in fails or proves impossible, the receiving participant can choose to be paid cash compensation or to defer execution of the buy-in. All buy-in costs are to be borne by the failing participant.

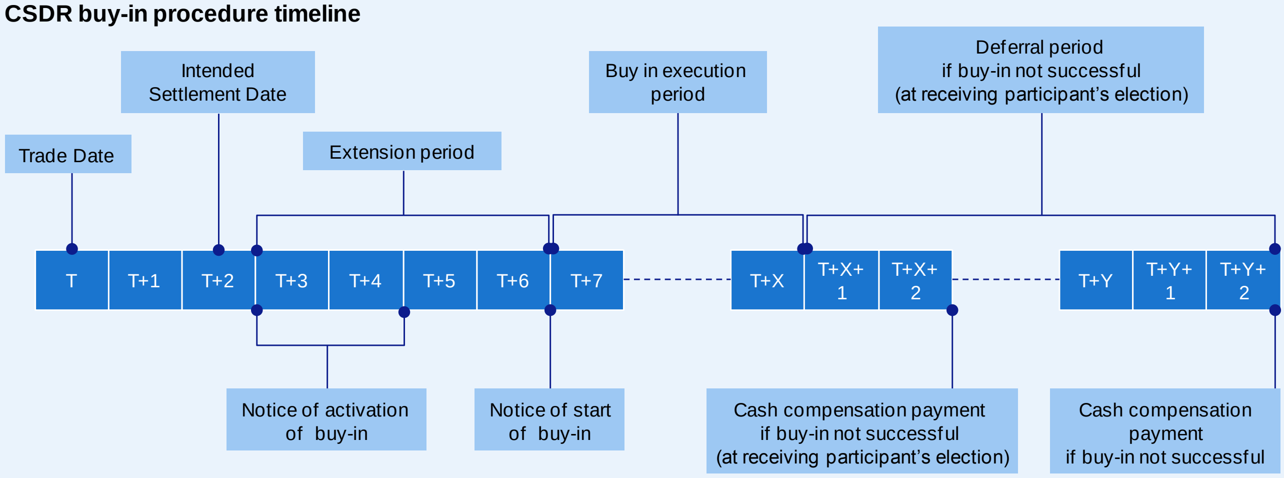
Although the obligation to establish procedures to remedy settlement failure (including through buy-in) falls on CSDs, the effectiveness of these procedures is critically dependent on cooperation with trading venues and, potentially, CCPs. After all, a SSS *per se* is not a place where securities are "bought or sold" but simply a system in which payment and delivery obligations associated with transactions executed elsewhere (either on or off venue) may be discharged. The Regulation requires CSDs to consult with the trading venues and CCPs for whose markets they provide SSSs before establishing settlement failure procedures and provides that for transactions that are centrally cleared, the relevant CCP acts as the entity that executes the buy-in. For transactions that are not centrally cleared but which are executed on venue, the venue itself is required by the Regulation to include obligations in its rules compelling venue participants to fulfil the Regulation's buy-in requirements.

Finally, for transactions that are neither centrally cleared, nor executed on a venue (which may include not insignificant volumes of cash equities trades in some markets) the Regulation requires CSDs to frame their rules so that *the CSD participants* are subject to the buy-in requirements contemplated by the Regulation. The latter point is potentially alarming for the banks and custodians who act as settlement agents in SSSs but do not offer a "Model B" service. The custodian or settlement agent who participates in the CSD quite likely has nothing to do with the execution of the transaction that failed to settle. Execution will have involved different entities altogether and unless the executing broker is proprietary trading, probably has no economic interest in the transaction (apart from its fee) either. Placing any responsibility for settlement discipline on CSD participants in these circumstances is rather like holding the post office responsible for ensuring delivery of a parcel from an online retailer in instances where the retailer itself failed to put the item in the post in the first place. It would have been helpful if the legislator had stated unambiguously that the legislation does not, and is not intended to make settlement agents the guarantors of transaction counterparties.

The Regulation does require ESMA to draft RTS on the settlement discipline procedure. One hopes that that rule making process clarifies that the impact of the Regulation for custodians and settlement agents. Whilst such entities might voluntarily be assuming credit risk on their clients in their contracts with them, it is imperative that the Regulation should not impose additional legal obligations on custodians and settlement agents to honour the payment and delivery obligations of their defaulting clients. Once the relevant Level 2 measures have finalized the design of the Regulation's settlement failure regime, exchanges and market participants will need to change their rules and contracts to reflect the new regime to the extent that the regime deviates (as seems possible) from existing industry and contractually agreed buy-in procedures.

In many cases, settlement failure is unlikely to be to be the fault of the CSD participants but more likely to be caused by the default of participants' clients. CSD participants who are penalised under the new settlement failure regime may seek to push the costs of penalties down the transaction chain to their clients where they consider the failure to be the client's fault.

CSDR buy-in procedure timeline



Securities holding and issuance

The Regulation mandates the recording in book entry form of all securities admitted to trading on an RM, MTF or OTF. This can be achieved either via immobilisation (where a paper security exists but is held in global form by a depository linked to a settlement system) or through full dematerialization (i.e. the total elimination of paper certificates or documents of title such that the security only exists as a computer record). Given the existing prevalence of dematerialization these requirements may be of little practical consequence in most member state markets – though undoubtedly there will be some markets affected.

The Regulation establishes in European law a freedom for EU securities issuers to choose any EU CSD to record securities that are traded on a venue. This "freedom to issue" is without prejudice to the governing law of the instrument itself. It is noteworthy that the Regulation does not attempt to resolve questions of securities ownership and could lead to even more complex conflicts of laws questions by creating potential for increasing numbers of the following type of scenario: e.g. a Latvian entity issuing English law governed bonds in an Italian CSD held in custody by a French custodian or the EU branch of a US custodian.

The "freedom to issue" is not absolute. While CSDs are required to treat requests for recording in a non-discriminatory manner, they can refuse to provide services to an issuer following a comprehensive risk assessment or in cases where the CSD does not provide recording services for securities issued under the relevant governing law of the instrument.

> The freedom for EU securities issuers to choose any EU CSD to record securities could lead to even more complex conflicts of laws questions.

Authorization and supervision of CSDs

In a process analogous to the re-authorization of CCPs under EMIR, the Regulation will require European CSDs to become authorized by national competent authorities. The Regulation allows Member States to designate one or more competent authorities to carry out the authorization and supervision of CSDs although the following are all required to be involved in the process: (a) the authority responsible for oversight of the SSS operated by the CSD (e.g. the Bank of England in relation to CREST); (b) the central banks issuing the most relevant currencies in which settlement takes place (e.g. the Rijksbank for systems settling in SEK); and (c) where relevant, the central bank in whose books the cash leg of a securities settlement system operated by a CSD is settled (e.g. Bank of Greece for settlement of Greek government debt in the BOG system).

The authorisation process establishes the scope of services (see table below) that a CSD can provide. All applicants are required to submit their application to the competent national authority which then has 30 days to determine the completeness of the application. The deadline for CSD re-authorization applications will be six months from the entry into force of relevant technical standards. Drafts of those technical standards will go to the Commission by 15 June 2015 and it is likely that they will enter into force towards the end of 2015 or early in 2016, giving a possible authorization application deadline some time in mid-2016. Once completeness has been determined, the regulator has a further 6 months to consider the application, during which period it will liaise with other relevant regulators (including in different member states where the CSD in question is a sister company, subsidiary of or otherwise controlled by a CSD authorized in another member state). If the CSD will provide any MiFID 2 "investment services" then the competent authority under MiFID 2 would also be consulted. ESMA will keep a register of authorized CSDs similar to the register of CCPs that it maintains under EMIR.

The Regulation states that only CSDs authorised under the Regulation are permitted to operate an SSS. This is presumably not intended to exclude the operation of SSS by recognised third country CSDs. If a CSD wishes to provide "banking-type ancillary services" (i.e. providing cash accounts, overnight cash credit lines, payment services (including foreign exchange), guarantees for securities lending/borrowing and treasury management services) then it must obtain an additional authorization. Direct provision by the CSD of bank-type ancillary activities requires the CSD to be an authorized credit institution under the Banking Directives and to satisfy additional prudential requirements under Title IV of the Regulation. Regulatory approval is required for the outsourcing of "core functions" (see table below) by authorised CSDs and CSDs that outsource services remain fully responsible for discharging their obligations under the Regulation.

Organisation and governance

The Regulation subjects CSDs to governance requirements analogous to those imposed on CCPs under EMIR. These include requirements for a clear organisation structure and reporting lines, a 10 year record keeping requirement, maintenance of conflicts of interest policies and controls designed to ensure the fitness and propriety of senior management and suitability of shareholders. CSDs are also required to establish an independent user committee for each SSS they operate, composed of securities issuers and SSS participants.

Conduct of business

The main conduct of business rules for CSDs under the Regulation include open and non-discriminatory access requirements, complaints handling procedures, public disclosure of prices and fees and other transparency requirements that *inter alia* enable the CSD's clients to assess the risks associated with the services provided.

CSD Services and Segregation

The Regulation establishes various obligations on CSDs to ensure the integrity of securities issues (such as reconciliation processes and prohibitions on securities overdrafts or debit balances in non-cash accounts at the CSD) and to reduce the risks associated with the safekeeping and settlement of securities transactions.

In a provision that echoes Article 39 of EMIR, the Regulation imposes an obligation on the CSD to keep records and accounts that enable it to segregate in its accounts the securities of one participant from another and, if applicable, from the CSD's own assets as well. CSDs are also required to keep records and accounts that enable participants to segregate their proprietary securities from those of their clients and to facilitate the offering by participants to their clients of a choice between 'omnibus' and 'individual' client account segregation. CSD participants are required to warn their clients of the different costs, risks and benefits associated with each option. One difference from Article 39 of EMIR however is the omission in the Regulation of a requirement to record the client's selection in writing. Thus, participants may simply make the offer of individual segregation and, it would appear, if a client does not positively select individual segregation, the participant may continue to provide omnibus segregation.

The obligations relating to segregation that are imposed under the Regulation only affect CSDs and their participants. They do not attempt to ensure complete segregation throughout a potentially long chain of different intermediaries. Effective segregation requires a similar level of account segregation to be maintained by every intermediary in the holding chain. However, the Regulation is concerned, at most, with two levels of intermediary; the CSD and the participant. Within the EU, where other intermediaries in the holding chain are subject to similar segregation requirements (such as clearing members under EMIR) then the integrity of the segregation throughout the chain is promoted. However, the interposition in the chain of a non EU intermediary not subject to similar segregation obligations could disrupt segregation. Given the narrow scope of the segregation obligations under the Regulation, its provisions can be seen as less ambitious than those under the draft Securities Law Legislation (an instrument that remains on the legislative back burner). Early drafts of the latter introduced wide ranging concepts of account holder and provider that would catch far more intermediaries than the CSDs and participants affected by the Regulation. However, those intermediaries who are affected by the Regulation (e.g. custodians participating directly in a CSD) may owe fiduciary obligations to their own clients (not all of whom will necessarily have the status of "indirect participants" in the CSD) and may need to make their clients aware of the different types (and associated service costs) of client account segregation available at the level of the CSD and seek their client's instructions as to the desired account type.

The Regulation requires all SSS operated by CSDs to be designated pursuant to the Settlement Finality Directive (the SFD). CSDs themselves are required to specify the moments of entry and irrevocability of transfer orders clearly in their rules and to take reasonable steps to ensure that finality of cash and securities transfers is achieved either in real-time, or intra-day on the intended settlement date and no later than settlement date plus 1. Reflecting an important CPSS-IOSCO core principle, cash legs of settlements are required, where possible, to settle in central bank money (i.e. across accounts at the central bank that issues the relevant settlement currency) rather than in commercial bank money which is an inherently riskier settlement asset. Where settlement in central bank money is not practical or available, the Regulation permits settlement of the cash leg in the CSD's own accounts or the accounts of a commercial bank, in each case subject to the Regulation's additional prudential requirements under Title IV. The Regulation places strict controls that limit the scope for a CSD to provide cash settlement or other banking type activities from within the same entity that operates an SSS or from a separate entity in the same CSD group. Furthermore, if a CSD sought to designate a third party to perform these activities, the Regulation would require the establishment of a stand-alone, fully capitalised credit institution licensed only to perform cash settlement or other banking type activities for CSDs, which may not be an attractive proposition for fully independent banks.

To manage participant default, the Regulation requires that CSDs have clearly defined and publicly available participant default rules though the Regulation does not explain how these would interact with the default rules of other market infrastructure (such as CCPs and trading venues) which – if the SSS participant is also a trading or clearing member of a venue or CCP – may also be relevant in their default.

Cash legs of settlements are required, where possible, to settle in central bank money... if a CSD appoints a third party commercial bank to perform cash settlement, the Regulation requires the establishment of a stand-alone, fully capitalised credit institution licensed only to perform CSD cash settlement... which may not be an attractive proposition for fully independent banks.

CSD Services (Annex to the Regulation)

SECTION A
Core services of central securities depositories

1. Initial recording of securities in a book-entry system ('notary service');
2. Providing and maintaining securities accounts at the top tier level ('central maintenance service');
3. Operating a securities settlement system ('settlement service').

SECTION B
Non-banking-type ancillary services of CSDs that do not entail credit or liquidity risks

Services provided by CSDs that contribute to enhancing the safety, efficiency and transparency of the securities markets, which may include but are not restricted to:

1. Services related to the settlement service, such as:
   (a) Organising a securities lending mechanism, as agent among participants of a securities settlement system;
   (b) Providing collateral management services, as agent for participants in a securities settlement system;
   (c) Settlement matching, instruction routing, trade confirmation, trade verification.
2. Services related to the notary and central maintenance services, such as:
   (a) Services related to shareholders' registers;
   (b) Supporting the processing of corporate actions, including tax, general meetings and information services;
   (c) New issue services, including allocation and management of ISIN codes and similar codes;
   (d) Instruction routing and processing, fee collection and processing and related reporting.
3. Establishing CSD links, providing, maintaining or operating securities accounts in relation to the settlement service, collateral management, other ancillary services.
4. Any other services, such as:
   (a) Providing general collateral management services as agent;
   (b) Providing regulatory reporting;
   (c) Providing information, data and statistics to market/census bureaus or other governmental or inter-governmental entities;
   (d) Providing IT services.

SECTION C
Banking-type ancillary services

Banking-type services directly related to core or ancillary services listed in Sections A and B, such as:

(a) Providing cash accounts to, and accepting deposits from, participants in a securities settlement system and holders of securities accounts, within the meaning of point 1 of Annex I to Directive 2013/36/EU (CRD IV);
(b) Providing cash credit for reimbursement no later than the following business day, cash lending to pre-finance corporate actions and lending securities to holders of securities accounts, within the meaning of point 2 of Annex I to Directive 2013/36/EU (CRD IV);
(c) Payment services involving processing of cash and foreign exchange transactions, within the meaning of point 4 of Annex I to Directive 2013/36/EU (CRD IV);
(d) Guarantees and commitments related to securities lending and borrowing, within the meaning of point 6 of Annex I to Directive 2013/36/EU (CRD IV);
(e) Treasury activities involving foreign exchange and transferable securities related to managing participants' long balances, within the meaning of points 7(b) and (e) of Annex I to Directive 2013/36/EU (CRD IV).

Prudential requirements

Under the Regulation, CSDs are required to adopt a sound risk management framework to manage legal, operational and other risks, including measures to mitigate fraud and negligence. CSDs are required to hold capital (together with retained earnings) that is proportionate to the risk stemming from their activities. Capital is required at all times to be sufficient to ensure the CSD is continually able to provide services as a going concern and to ensure an orderly wind-down or restructuring over at least 6 months in a range of stress scenarios. CSDs are also required to maintain plans to raise extra capital when needed and to ensure orderly wind-down if the CSD is unable to recapitalize. For CSDs that are banks and that will provide "banking-type" ancillary services, Title IV of the Regulation establishes more detailed and rigorous "bank-like" prudential requirements.

In terms of investment policy, the Regulation restricts CSDs to holding their financial assets with central banks, authorised commercial banks or authorised CSDs and to investing only in cash or highly liquid financial instruments with minimal market and credit risk. The Regulation also requires CSDs to limit their exposure to any one institution via "acceptable concentration limits". ESMA (in conjunction with the EBA and the members of the ESCB) is tasked with specifying through technical standards the detail around these investment restrictions.

Passport

Once authorised, EU CSDs will be have a passport to provide CSD services in other member states (including via branches). Use of the passport first requires the CSD to communicate the scope of its intended cross-border activities to its home state regulator who will, in turn, pass on the information to the host state regulator. However, prior to doing so, the home state regulator has the power, where it has doubts as to the administrative structure or financial situation of the CSD concerned, to prevent the use of the passport by declining to liaise with the host state regulator. If the home state regulator exercises this power to refuse, it must give written reasons to the CSD concerned. In the absence of such a block, the CSD can begin to provide services in the host member state once: (a) it has received confirmation from the host state regulator that it has received the relevant information from the home state regulator; or (b) if the host state regulator does not provide such confirmation, within three months of the home state regulator sending the relevant information to its host state counterpart.

For CSDs operating in multiple member states, the Regulation envisages a framework for ongoing cooperation and information exchange between home and host authorities. Where a CSD's activities become of "substantial importance" to securities markets and investor protection in a host state, the Regulation requires cooperation arrangements be put in place between the home and host authorities, potentially including colleges of supervisors. The criteria for establishing "substantial importance" are to be specified by the Commission through delegated acts Unfortunately, it is not immediately obvious what will constitute "provision of services within the territory of another member state".

Third country CSDs

The Regulation permits third country CSDs to provide CSD services within the EU, including via branches. EU CSDs are also permitted to establish links with third country CSDs. Third country CSDs that wish to provide either notary or central maintenance services in relation to securities whose governing law is that of an EU member state or that wishes to establish an EU branch are required to apply for recognition from ESMA which is itself dependant (*inter alia*) on the Commission having adopted a determination as to the equivalence of the CSD supervision, oversight and enforcement regime in the third country.

CSD Links and other market infrastructure

A CSD link is an arrangement between CSDs where one CSD becomes a member of another CSD's SSS to enable transfers of securities between participants of the different CSDs. The Regulation envisages four different types of link:

- Standard link: a CSD participates in the SSS of another CSD on the same terms as any other participant;
- Customised link: a CSD that participates in the SSS of another CSD is provided with services additional to those that the other CSD provides its normal participants;
- Indirect link: an arrangement between a CSD and a non-CSD third party who is a participant in the SSS of another CSD;
- Interoperable link: a CSD link where CSDs establish mutual technical solutions for settlement in the SSSs that they operate.

CSDs that intend to establish links are required by the Regulation to apply for authorisation from the regulator of the requesting CSD. Any link is required to provide "adequate protection" to both CSDs and their participants, in particular regarding credits between the CSDs and the concentration and liquidity risks that the arrangement could produce. Links are also required to be supported by appropriate contractual arrangements to include unambiguous choice of law provisions governing the link's operations. Links are to permit delivery versus payment settlement for transactions between participants in linked CSDs and notification to the competent authorities is required in the event that DVP is not supported by the link. Delineating the "adequacy" of protection arrangements and other important elements relating to CSD links will fall to ESMA, who is tasked with developing technical standards in this area in cooperation with the members of the ESCB.

Changes to other legislation

The Regulation makes a number of technical amendments to other legislation including MiFID 2, MiFIR and the SFD. The Regulation also deletes the buy-in provisions under Article 15 of the Short Selling Regulation – a move that had met with industry opposition since it may mean that CCPs need to review their current buy-in procedures now, even before the Regulation's new settlement discipline measures take effect (which is not expected before late 2015 / early 2016).

Target 2 Securities

The Regulation is also a key development towards achieving the broader goals of the Target 2 Securities (T2S) project. Scheduled to go live during 2015, T2S is a proposal by the European Central Bank (ECB) to provide a central settlement function for the euro area, with other European currencies invited to join (though the UK has declined to and sterling will not be a T2S currency). T2S is a "settlement platform" (not a CSD). It aims to streamline the landscape for the settlement of cross-border transactions in the EU and to improve the efficiency and security of settlement for European securities transactions.

Notes

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