ECSDA
European Central Securities Depositories Association

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ECSDA Comments on the upcoming Level 2 measures related to CSD authorisation under the CSD Regulation

This paper constitutes the second part of ECSDA's response to the ESMA consultations of 18 December 2014 on technical standards (covering questions 15 to 31), technical advice (questions 5 to 8) and guidelines (1 question) under the CSD Regulation. The full consultation response was submitted to ESMA on 19 February 2015 using the mandatory reply form. This version of the document includes an executive summary and is intended for public circulation.

Amendment proposals included in this paper are presented in italics, with suggestions for additional wording in ***bold italics,*** and suggestions for deletions marked by ***~~a strikethrough~~***.

Executive Summary

Technical standards, technical advice and guidelines to be issued by ESMA in June 2015 in relation to the CSD Regulation (CSDR) are very important to ensure that the objectives of the EU legislator are met, and that the regulatory framework for central securities depositories (CSDs) is implemented consistently across Europe, contributing to a safe, efficient and competitive post trade landscape.

European CSDs have analysed the ESMA Consultation Paper in detail and, as far as the CSD authorisation requirements are concerned, we have identified some important issues that need to be solved prior to the finalisation of "Level 2 legislation".

- First, the proposed record keeping requirements are too far-reaching and would impose obligations on other entities than CSDs, including CSD account holders and issuers as regards the obligation to obtain a Legal Entity Identifier (LEI). Without denying the benefits of using LEIs, CSDs are concerned that they will not be able to impose their use by third parties, especially when these are established outside the European Union. There is thus a risk that CSDs will be unable to comply with the ESMA standards in practice.

As a result, ECSDA is convinced that the draft standards on record keeping must be recalibrated and that ESMA should:

(a) allow CSDs to keep their records in the current format and, if a certain format is mandated in the technical standards for the purpose of regulatory reporting, ensure that this format is compatible with global ISO standards;
(b) only require CSDs to maintain those records they need to provide services;
(c) not confuse CSD records with the type of data that CSDs need to maintain to resume activities in case of operational problems as part of their business continuity policy;
(d) refrain from imposing the record keeping requirements in a retro-active way, so that only records maintained by CSDs after they have been authorised under the CSDR - and after the record keeping requirements have entered into effect - are assessed against the new requirements;
(e) foresee a phased-in implementation for record keeping requirements, in line with the phase-in for settlement discipline measures, i.e. ideally for a period of at least 24 months after the ESMA technical standards enter into force. Such phase-in should apply at a minimum for those records linked to settlement discipline information and to the use of LEIs for reporting purposes.

- Second, ECSDA wishes to stress the importance of allowing CSDs to continue to maintain links with non-EU CSDs. Expecting CSDs or intermediaries established in non-EU jurisdictions to be subject to a comparable regulatory regime to that in place in the EU is not realistic given that European rules are among the strictest in the world. It is also not justified from a risk perspective since CSD links do not expose the linked CSDs to credit risk. Forcing European CSDs to discontinue existing links with non-EU CSDs would be detrimental to market integration and would not in any way enhance the safety of cross-border settlements, since transactions would have to occur outside the network of existing infrastructures. It is thus important that the technical standards on CSD links be recalibrated to take into account the need to maintain access to non-EU markets.

- Third, the proposed reconciliation rules need to be adapted in two ways to avoid negative consequences for financial stability:

(a) Suspension of settlement in a financial instrument should not be automatic in case of discrepancies identified during the reconciliation process. There should be an element of proportionality to ensure that the damage caused by the suspension is not greater than that caused by the reconciliation error;
(b) Requirements on daily reconciliation should only apply to cases where the CSD provides central maintenance services for a financial instrument. In other cases, including in the case of offshore investment funds for which a transfer agent provides the notary and central maintenance services, the CSD is not in a position to impose daily reconciliation to the third party transfer agent and can only perform reconciliation as any other intermediary in the chain. Taking such cases into account is fundamental to avoid that CSDs are forced to discontinue their services in such markets - services which contribute to reduce risk and support settlement efficiency for market participants.

1. Responses to the ESMA consultation questions (technical standards)

A. CSD authorisation, supervision and recognition

Q15: What are your views on the proposed draft RTS on CSD authorisation (Chapter II of Annex II) and draft ITS on CSD authorisation (Chapter I of Annex VI)?

This question refers to:
Section 3.1 of the Consultation Paper (p.38-43)
Annex 2 Chap. 2 (p.158-176): draft RTS
Annex 6 Chap. 1 (p.260-261): draft ITS

1) Comments on the draft RTS (Annex II, Chapter II)

- **Definition of the "review period" (art.1 RTS, p.158)**

ECSDA agrees with the proposed definition of the review period. We expect that, by default, competent authorities will carry out annual reviews each calendar year.
Although we are aware that individual CSDs will very likely be granted an authorisation at different points in time, ECSDA favours a harmonisation of the review periods based on the calendar year whenever possible (e.g. at the start of the calendar year following which the authorisation has been granted). Such a frequency would have the advantage of being aligned with the period for which statistical data is to be provided by CSDs under art.42(2) of the draft RTS (p.180-181).

- **General information to be provided on the applicant CSD (art.2 RTS, p.159-160)**

ECSDA generally agrees with the list of information items contained in article 2 of the draft RTS which should be provided by CSDs as part of their application file. Nonetheless, we would like to recommend a few clarifications:

- As regards art.2(1), we think that the word *"activities"* should be replaced by *"services"*, in line with the terminology used in the Level 1 CSD Regulation;
- As regards art.2(2)(m), we recommend clarifying that CSDs should only provide information on services regulated under MiFID when these are not already covered by the Annexes of the CSD Regulation;
- As regards art.2(2)(n), we recommend referring explicitly to all core and ancillary services outsourced by a CSD to a third party since this information is relevant for authorisation purposes;
- As regards art.2(2)(o), the notion of currencies "*being processed*" by CSDs should be further specified to ensure a clear and consistent interpretation by all competent authorities. ECSDA assumes that the intention of ESMA is to obtain information on the list of currencies used for DvP settlement on cash accounts held either at a central bank, at the CSD itself (if the CSD has obtained a banking authorisation) or at a designated credit institution. In order to confirm this interpretation, we recommend adding more specific language to art.2(2)(o).

ECSDA recommends amending art.2 of the draft RTS as follows:

Article 2 - Identification and legal status of a CSD
1. An application for authorisation of a CSD shall identify the applicant and the ***services*** ~~***activities***~~ *that it intends to carry out.*
[…] 2. The application for authorisation of a CSD shall in particular contain the following information:
[…] (m) where applicable, the list of any services and activities that the CSD is providing or intends to provide under Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments ***which are not expressly listed in Sections A and B of the Annex to Regulation (EU) No 909/2014"****;*
(n) of the list of ~~***any***~~ ***core or ancillary services*** *outsourced* ~~***services***~~ *to a third party under Article 30 of Regulation (EU) No 909/2014;*
(o) the currency or currencies it processes, or intends to process ***as part of the settlement service, irrespective of whether cash is settled on a central bank account, a CSD account, or an account at a designated credit institution;***

- **CSD policies and procedures (art.3 RTS, p.160-161)**

ECSDA recommends amending art.3 of the draft RTS as follows:

Article 3 - Policies and procedures required under this Regulation
1. Where an applicant CSD is required to provide information regarding its policies or procedures under this Regulation, it shall ensure that the policies or procedures contain or are accompanied by each of the following items:
(a) an indication of the ~~***persons***~~ ***department(s)*** *responsible for the approval and maintenance of the policies and procedures;*
(b) a description of how compliance with the policies and procedures will be ensured and monitored, and the ~~***person***~~***department*** *responsible for compliance in that regard;*
(c) a description of the ***type of*** *measures to adopt in the event of a breach of policies and procedures.*
*[…] 2. An application for authorisation shall contain the procedure****s or a description of the procedures in place for employees to report internally actual or potential infringements of*** ~~***for reporting to the competent authority any material breach of policies or procedures of a CSD, in particular when such infringement may result in a breach of the conditions for initial authorisation, as well as in any infringement of***~~ *Regulation (EU) No 909/2014 in accordance with Article 65 of Regulation (EU) No 909/2014.*

Indeed, we believe that identifying a department or departments is more appropriate than identifying a single person in the context of art.3(1)(a) and (b) given the way CSDs operate. Relying on a department would in particular guarantee some continuity in case of changes in the staff of the CSD.

As regards article 3(1)(c), we believe that, given the number of policies and procedures typically maintained by a CSD, it is more workable for a CSD to put in place a general framework determining "types" of measures, rather than individual measures, in case of a breach in one of the policies or

procedures. Having a separate list of measures for each policy and procedure would be too burdensome to maintain and is not necessary, as long as the framework applies to all policies and procedures.

Furthermore, we believe that our proposed amendment to art.3(2) would make the draft RTS more closely aligned with the Level 1 text of the CSD Regulation, given that articles 26(5) and 65(3) of the CSDR lay down the internal "whistle-blowing procedures" that CSDs have to put in place, whereas the procedure for reporting breaches to the competent authority is laid down by the authority itself, not the CSD.

- **Information for groups (art.4 RTS, p.161)**

ECSDA welcomes the inclusion by ESMA of an article recognising the specificities of corporate group structures in the draft RTS. That said, we believe that the first sentence of the article should be rephrased to be more closely aligned with art.26(7) of the CSDR which restricts the provision of detailed information on policies and procedures to cases where there are one or more CSDs and/or credit institutions in the corporate group to which the CSD belongs. The phrase *"in particular"* currently suggests information might be provided in other cases and thus goes beyond the Level 1 text.

As regards art.4(1)(b), we assume that ESMA wishes the competent authority to obtain information on the parent company and other relevant group entities (other CSDs or credit institutions), rather than on all entities of the group. We thus recommend amending the article to specify more clearly in relation to which group entities the information should be provided.

As regards art.4(3), ECSDA understands that ESMA wishes the competent authority to obtain information on other group entities which might perform Section B services (e.g. registrar services) for a CSD, without that these entities be themselves authorised as CSDs. We thus find the phrase *"or through an undertaking with which the applicant CSD has an agreement"* confusing and unnecessary. In cases where outside (non-group) entities provide ancillary services (e.g. registrar services) in the market where a CSD operates, these services are by definition not offered by the CSD itself, and so it is hard to imagine how a CSD could *"offer or plan to offer"* services via such an entity. Given that the activities of such non-group entities are anyways outside of the scope of art.4 of the draft RTS, which is meant to cover *"information for groups"*, we suggest removing this phrase from art.4(3).

Article 4 - Information for groups

1. Where an applicant CSD is part of a group of undertakings ***which*** *includ****esing*** ~~***in particular***~~ *other CSDs and credit institutions referred to in Title IV of Regulation (EU) No 909/2014, the application for authorisation shall contain the following items:*

(a) policies and procedures specifying how the organisational requirements apply to the group and to the different entities of the group, from the perspective of the interaction with the applicant CSD;

(b) information on the composition of the senior management, management body and shareholders of the parent undertaking or ***any other CSD and credit institutions belonging to the same*** *group of undertakings;*

(c) services as well as key individuals other than senior management that are shared by the group.
2. Where the applicant CSD has a parent undertaking, the application for authorisation shall additionally:
(a) identify the legal address of its parent undertaking;
(b) indicate whether the parent undertaking is authorised or registered and subject to supervision, and when this is the case, state any relevant reference number and the name of the competent authority or authorities.
3. Where the applicant CSD offers, or plans to offer, through an undertaking within its group, ***~~or through an undertaking with which the applicant CSD has an agreement~~****, ancillary services permitted under section B of the Annex to Regulation (EU) No 909/2014, the application for authorisation as CSD shall contain a description of the respective ancillary services.*
4. Where the applicant CSD has an agreement with an undertaking within the group relating to the offering of trading or post-trading services, the application shall contain a description and a copy of such agreement.

- **Financial resources (art.5 RTS, p.162-163)**

Art.5(1)(a) and (b) of the draft RTS include a reference to specific accounting standards and financial reporting standards to which not all CSDs are subject today. Given that there is no mention of these accounting and financial reporting standards in the CSDR, and in the absence of a mandate for ESMA to harmonise CSDs' accounting standards, ECSDA believes that the draft RTS should not impose additional requirements on CSDs, especially as the CSDR requirements can be fulfilled by relying on existing accounting and financial reporting standards used by CSDs (and agreed with competent authorities).

As regards art.5(1)(d) of the draft RTS, ECSDA is not convinced that the requirement for CSDs to include a business plan in their application for authorisation is necessary in the case of already established CSDs. We believe that contemplating different business scenarios for CSD services over a 3-year period makes sense for newly established CSDs, but that it is unlikely to provide any important new elements to competent authorities already aware of the business plans of existing CSDs under their supervision.

ECSDA thus suggests amending art.5(1) of the draft RTS as follows:

Article 5 - Financial reports, business plans, recovery plans and resolution plans
1. An application for authorisation of a CSD shall contain the following financial and business information about the applicant CSD:
(a) a complete set of financial statements, ***~~prepared in conformity with Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards~~****, for the preceding three years;*
(b) financial reports including the statutory audit report on the annual and consolidated financial statements, ***~~within the meaning of Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts~~****, for the preceding three years,*
[…] (d) ***for newly established CSDs not yet operating under the supervision of the competent authority****, a business plan, including a financial plan and an estimated budget, contemplating different business scenarios for the CSD services, over a minimum of three years reference period.*

The draft RTS provide helpful guidance on the structure and contents of the recovery plan that CSDs must submit to their competent authority. However, art.5(5)(b) also requests the submission by the CSD of *"the resolution plan established and maintained by the CSD".* ECSDA believes that the current formulation in the draft RTS is misleading and should be amended.

Indeed, unlike recovery plans, which are drafted and maintained by CSDs, resolution plans are the responsibility of public authorities, as acknowledged by CSDR article 22, the CPMI-IOSCO Principles for financial market infrastructures (PFMI)[1] and the FSB Key Attributes[2]. Asking a CSD to provide its resolution plan to the competent authority goes against the principle that the resolution plan is to be drafted and maintained by the resolution authority, not the CSD. It also assumes that CSDs have access to their own resolution plan, which might not always be the case, given that there is no obligation for a resolution authority to communicate its resolution plan to a CSD (including when the plan is updated). In fact, some authorities might even find it is undesirable for a CSD to have access to its resolution plan. The current approach for the recovery and resolution of financial institutions is that it is the competent authority's duty to verify and provide all available information relevant for resolution planning to the resolution authority - where the authorities are different institutions - and the financial institution on the other hand has a duty to cooperate and provide information *"directly or indirectly through the competent authority",* as stated for instance in article 11 of the BRRD (Directive 2014/59/EU).

A better way to ensure that the competent authority of the CSD has a copy of the CSD's resolution plan is thus to (a) require CSDs to provide the competent authority with all the information necessary for the resolution authority to draw up or update the resolution plan, and (b) to require the resolution authority to provide the resolution plan to the competent authority of the CSD, when the resolution authority is different from the competent authority.

ECSDA thus suggests either deleting art.5(5)(b) of the draft RTS or amending it as follows:

Article 5 - Financial reports, business plans, recovery plans and resolution plans

[…] 5. The application shall also include:

[No changes to point (a)]

~~(b) the resolution plan established and maintained for the CSD so as to ensure continuity of at least its core functions, having regard to the size, systemic importance, nature, scale and complexity of the activities of the CSD concerned.~~

(b) any information deemed necessary to ensure that the resolution plan established and maintained by the resolution authority ensures the continuity of at least the CSD core functions, having regard to the size, systemic importance, nature, scale and complexity of the activities of the CSD concerned."

[1] CPSS (now CPMI) and IOSCO, Principles for financial market infrastructures, April 2012: http://www.bis.org/cpmi/publ/d101.htm

[2] FSB, Key Attributes of Effective Resolution Regimes for Financial Institutions, 15 October 2014: http://www.financialstabilityboard.org/2014/10/r_141015/

Such an amendment would require ESMA to include a definition of "resolution authority" and to clarify the responsibilities of authorities in line with global standards.

We believe that the amendment we suggest would make the RTS fully compatible with the Level 1 CSDR and global standards on the resolution of financial market infrastructures:

- Principle 3 of the PFMI, in its Key Consideration 4, states that *"where applicable, an FMI should also provide relevant authorities with the information needed for purposes of resolution planning";*
- The FSB Key Attributes, which include in Appendix II, Annex 1, specific guidance for the resolution of financial market infrastructures like CSDs, further state that *"jurisdictions should require that the firm's senior management be responsible for providing the necessary input to the resolution authorities for (i) the assessment of the recovery plans; and (ii) the preparation by the resolution authority of resolution plans";*
- Finally, CSDR article 22(3) clearly states that the competent authority, not the CSD, "*shall ensure that an adequate resolution plan is established and maintained for each CSD so as to ensure continuity of at least its core functions".*

- **Corporate governance (art.8 RTS, p.164)**

ECSDA recommends deleting point (b) from art.8(1) of the draft RTS given that risk management procedures are not part of corporate governance and rather relate to other (prudential) requirements under the CSDR:

Article 8 - Corporate governance
1. An application for authorisation of a CSD shall contain in accordance with Article 26 of Regulation (EU) No 909/2014 and the respective RTS:
[No changes to (a)]
[…] ~~***(b) the processes to identify, manage, monitor and report the risks to which the applicant CSD is or might be exposed.***~~

- **Board, senior management and shareholders (art.10 RTS, p.165-167)**

As regards the self-declaration of good repute required under art.10(1)(c), ECSDA would like to recommend amendments to points (vii) and (x) as follows:

Article 10 - Senior management, management body and shareholders
1. An application for authorisation of a CSD shall contain the following information in respect of each member of the senior management and each member of the management body, enabling the competent authority to assess the applicant CSD's compliance with Article 27(1) and (4) of Regulation (EU) No 909/2014:
[…] (c) a self-declaration of good repute in relation to the provision of a financial or data service, where each member of the senior management and the management body shall state whether they:

[…] vii. have been member of the management body or senior management of an undertaking which was subject to ***a sanction*** ~~***an adverse decision or penalty***~~ *by a regulatory body while this person was connected to the undertaking or within a year of the person ceasing to be connected to the undertaking;*
~~***[…] x. a declaration of any potential conflicts of interests that the senior management and the members of the management body may have in performing their duties and how these conflicts are managed.***~~

Indeed, as regards point (vii), the notion of "*adverse decision*" is unclear and potentially very broad, given that many undertakings have files pending with their regulators on a continuous basis. We thus recommend using the term "*sanctions*" instead. The notion of sanctions is less ambiguous and would cover any type of sanctions, including administrative fines, which an undertaking might have been subject to.
Moreover, point (x) appears misplaced as conflicts of interests are addressed under art.11 of the draft RTS and are not related to the notion of "*good repute*". We thus recommend its deletion.

- **Management of conflicts of interest (art.11 RTS, p.167-168)**

ECSDA agrees with the spirit of art.11 of the draft RTS on conflicts of interests but believes that the draft standards should be amended to provide more clarity on:

- **The notion of "disclosure" of conflicts of interests**: ECSDA understands that information on conflicts of interest should not be made publicly available, as it can contain sensitive and personal data on individuals, but should rather be communicated to the CSD's competent authority. A clarification of the notion of disclosure in art.11(1)(a) would thus be helpful. In particular, ECSDA understands that CSDs should only provide policies and procedures about how conflicts of interest are managed, identified and disclosed to their competent authority, without having to disclose each and every conflict of interest on an ad hoc basis. Such ad hoc disclosure would unnecessarily inflate the flow of information to the competent authority and might even prevent CSDs from addressing conflicts of interest once they emerge;
- **The resolution of conflicts of interests**: ECSDA believes that it is very difficult in practice to resolve "possible" conflicts of interests, as suggested in art.11(1)(c), and thus recommends that CSDs should submit to their competent authority resolution procedures in the event that actual conflicts of interests occur;
- **Register of conflicts of interest in the case of corporate groups**: In order to avoid misunderstandings, ECSDA recommends rephrasing art.11(2) to clarify that the register should include all conflicts of interest arising from other undertakings within the group that are related to the CSD activities. Indeed, other group entities will often not be subject to a similar requirement (maintaining a "register" of all conflicts of interests) and, even when they are, many of the conflicts of interests identified might be unrelated to the CSD's activity and thus unnecessary to be included in the application for authorisation.

ECSDA thus suggests amending art.11 of the draft RTS as follows:

Article 11 - Management of conflicts of interest
1. […] (a) policies and procedures with respect to the identification, management and disclosure ***to the competent authority*** *of conflicts of interest and a description of the process used to ensure that the relevant persons are aware of the policies and procedures;*
[no changes to (b)]
(c) resolution procedures whenever ~~***possible***~~ *conflicts of interest occur; […]*
2. Where the applicant CSD is part of a group, the register referred to in point (d) (ii) of paragraph 1 shall include any material conflicts of interest arising from other undertakings within the group ***in relation to CSD activities*** *and the arrangements made to manage these conflicts.*

- **Record keeping (art.14 RTS, p.169)**

See our answer under question 23.

- **Transparency (art.18 RTS, p.170)**

Under article 34 of the CSD Regulation, CSDs are required to *"publicly disclose the prices and fees associated with the core services listed in Section A of the Annex"*. As regards ancillary services, CSDs are only required to disclose to the competent authority *"the cost and revenue of the ancillary services provided as a whole"*. The different treatment of core and ancillary services under article 34 is the result of a political agreement of the EU legislator, and aims to avoid competitive distortions, since other market actors than CSDs can and do provide services listed in Section B or C of the Annex, without being subject to such transparency requirements.

ECSDA thus recommends that art.18 of the draft RTS should be amended as follows, to ensure full alignment with the Level 1 Regulation:

Article 18 - Transparency
1. An application for authorisation of a CSD shall contain relevant documents regarding pricing policy, including any existing discounts and rebates and conditions to benefit from such reductions for each core ~~***and ancillary***~~ *service*~~***s***~~ *that are to be disclosed in accordance with Article 34 of Regulation (EU) No 909/2014.*
2. The applicant CSD shall provide the competent authority with a description of methods used in order to make the information available for clients and prospective clients, including a copy of the ***published pricing policy for core services*** ~~***fee structure***~~ *and the evidence that the* ~~***CSD***~~ ***core*** *services are unbundled.*
3. The applicant CSD shall also provide the competent authority with information on the cost and revenue of ancillary services provided by the CSD, taken as a whole."

For the same reason, Recital (8) on page 155 of the Consultation paper should be amended as follows:

(8) The fees associated with the services provided by CSDs are important information which should form part of the application for authorisation of a CSD in order to enable the competent authorities to verify whether they ***comply***

with the conditions set under Regulation (EU) No 909/2014 ~~are proportionate, non-discriminatory and unbundled.~~

- **Book entry form (art.20 RTS, p. 170)**

ECSDA strongly believes that article 20 on the "book entry form" should be deleted from the draft RTS as the Level 1 CSD Regulation (article 3) does not impose any obligations on CSDs (only on issuers). It is actually impossible for CSDs themselves to enforce the book entry requirement, as suggested by the draft RTS, and article 4 of the CSDR further recognises this by clearly stipulating that regulators (issuers' regulators, trading venues' regulators, and regulators in charge of applying the Financial Collateral Directive), not CSDs, are responsible for enforcing the book entry requirement.

The proposed article 20 is thus unnecessary and inconsistent with the Level 1 text. It should be deleted entirely:

~~Article 20 - Book-entry form~~
~~An application for authorisation of a CSD shall contain information that demonstrates that the applicant CSD is capable to comply with Article 3 of Regulation (EU) No 909/2014.~~

- **Preventing and addressing fails (art.21 RTS, p. 171)**

Given the proposed "phase-in" for settlement discipline, art.21 of the draft RTS must be amended to make it clear that CSDs will only be required to provide information on compliance with the settlement discipline provisions of the CSDR once these provisions have truly entered into effect.

Art.21(b) also needs to be amended to reflect the fact that article 6(2) of the CSDR does not apply to CSDs, unlike article 6(3) and (4).

ECSDA thus suggests the following amendments to art.21 of the draft RTS:

Article 21 - Intended settlement dates and measures for preventing and addressing fails
As of the date of entry into force of Regulation (EU) No… [RTS on settlement discipline], ~~a~~A*n application for authorisation of a CSD shall contain the following information:*
(a) the rules and procedures that facilitate the settlements of transactions on the intended settlement date to in accordance with Article 6 of Regulation (EU) No 909/2014;
*(b) the details of mechanisms promoting early settlement on the intended settlement date and measures to encourage and incentivise the timely settlement of transactions by its participants in accordance with Article 6****~~(2) and~~*** *(3)* ***and (4)*** *of Regulation (EU) No 909/2014 and Regulation (EU) No… [RTS];*
(c) the details of the measures to address fails in accordance with Article 7 of Regulation (EU) No 909/2014 and Regulation (EU) No… [RTS].

- **"Portability" (art.27 RTS, p.172)**

ECSDA disagrees with the proposed title of article 27 of the draft RTS on "portability". We recognise the need for the draft RTS to further specify article 20(5) of the CSDR, but it is important to understand that the *"transfer of the assets of clients and participants to another CSD in the event of a withdrawal of authorisation"* is not a synonym for portability. In fact, the term "portability" was deliberately not included in the Level 1 CSD Regulation in recognition of the differences between CSDs and CCPs, in line with global standards. Indeed, Principle 14 of the PFMI on portability applies exclusively to CCPs, and deliberately so. Besides, whereas EMIR includes an article on portability (article 39) in the Level 1 text, there is no mention of the term "*portability*" in the Level 1 CSD Regulation. This is because transferring the positions of clearing members among competing CCPs presents specific challenges, which are different from those faced in the settlement context. We thus strongly believe that the term "*portability*" should not be introduced in the CSDR Level 2 standards, as it would create potential inconsistencies with the Level 1 CSDR and global standards, without bringing any benefits. We believe that the aims of art.27 of the draft RTS can be achieved by simply referring the *"transfer of participants and clients' assets"*, in line with the Level 1 terminology.

Furthermore, ECSDA recommends that art.27 of the draft RTS should be amended to give CSD participants a choice as regards the CSD to which their assets are transferred in case of a withdrawal of licence. If a CSD loses its licence, the continuity of critical services will be ensured under the recovery and resolution framework. Irrespective of the solution adopted (e.g. whether it involves transferring the notary and central maintenance services to another CSD or not), ECSDA believes that the failing CSD cannot impose the transfer of all participants' assets to a single CSD entity, and that CSD clients should be given the choice as to where they hold their assets as a result of the CSD losing its licence. The CSD's duty, on the other hand, is to ensure that such transfer of assets is possible and that it occurs smoothly according to participants' instructions, and with full respect of settlement finality rules. The issuer of the relevant securities should also be made aware of this procedure, especially in the case of cross-border transfers.

We thus suggest the following amendments to art.27 of the draft RTS:

*Article 27 – **~~Portability~~** **Transfer of participants and clients' assets in case of a withdrawal of authorisation***
*An application for authorisation of a CSD shall contain the procedure put in place by the applicant CSD in accordance with Article 20(5) of Regulation (EU) No 909/2014, ensuring the timely and orderly settlement and transfer of the assets of clients and participants to another CSD **of their choice** in the event of a withdrawal of authorisation of the applicant CSD.*

- **Operational risks (art.30 RTS, p.173)**

As regards art.30(2) of the draft RTS, ECSDA wonders whether ESMA intends to require CSDs to provide information on outsourcing arrangements for core services, as referred to in art.30(4) of the Level 1 CSDR, or on all material outsourcing arrangements covered by art.30 of the CSDR.

Given the lack of a precise definition of outsourcing and in order to avoid the inclusion of contracts with service providers which do not have any material impact on the performance of CSD functions (e.g. non-critical IT providers, consulting firms, payroll companies etc.), ECSDA recommends either limiting the requirements to outsourcing agreements for core services via a reference to art.30(4) of the CSDR, or alternatively introducing the notion of "*material*" outsourcing arrangements in art.30(2) of the draft RTS. This would be in line with existing requirements in place for financial institutions such as the 2006 EBA guidelines on outsourcing[3] which define outsourcing as *"an authorised entity's use of a third party (the "outsourcing service provider") to perform activities that would normally be undertaken by the authorised entity, now or in the future."* This definition illustrates that outsourcing typically implies the performance of services which are normally central to the activities of the authorised entity, i.e. CSD services as listed in Sections A to C of the Annex of the CSDR.

As a result, in order to achieve more clarity, we recommend amending art.30(2) of the draft RTS as follows:

Article 30 - Operational risks
[…] 2. An application for authorisation of a CSD shall also contain the information on ***material*** ~~***the***~~ *outsourcing agreements* ~~***referred to in Article 30 of Regulation (EU) No 909/2014***~~*, entered into by the applicant CSD* ***in accordance with Article 30 of Regulation (EU) No 909/2014****, together with the methods employed to monitor the service level of the outsourced functions and a copy of the contracts governing such arrangements.*

Or alternatively as follows:

Article 30 - Operational risks
*[…] 2. An application for authorisation of a CSD shall also contain the information on the outsourcing agreements referred to in Article 30****(4)*** *of Regulation (EU) No 909/2014, entered into by the applicant, together with the methods employed to monitor the service level of the outsourced functions and a copy of the contracts governing such arrangements.*

- **CSD services (art.33 RTS, p.174-175)**

ECSDA finds the first sentence of art.33 of the draft RTS confusing and recommends the following amendment:

[3] See http://www.eba.europa.eu/documents/10180/104404/GL02OutsourcingGuidelines.pdf.pdf

Article 33 - CSD Services
An application for authorisation of a CSD shall include ***a*** ~~***detailed***~~ *description*~~***s and procedures to be applied in the case***~~ *of* ***the*** *services that the CSD provides or intends to provide covering the following:*

- **CSD links (art.34 RTS, p.175)**

Assessing all potential sources of risks in the context of CSD links is not realistic and CSDs should be required to assess only all material sources of risk.

We thus recommend amending art.34(1)(a) as follows:

Article 34 - CSD Links
1. Where the applicant CSD has established or intends to establish a link, the application for authorisation shall contain the following information:
(a) procedures regarding the identification, assessment, monitoring and management of all ***material*** ~~***potential***~~ *sources of risk for the applicant CSD and for its participants arising from the link arrangement, including an assessment of the* ***relevant*** *insolvency law* ~~***applicable***~~*, and the appropriate measures put in place to mitigate them;*
[…]

2) <u>Comments on the draft ITS (Annex VI, Chapter I)</u>

ECSDA generally agrees with the proposed ITS. As regards art.1(5) of the draft ITS (stating that CSDs can be required by their competent authority to provide translations of their application documents in other languages), ECSDA would like to stress that such translations can be extremely costly to produce for CSDs (potentially exceeding EUR 100,000 for several hundreds of pages), and should only be requested for those documents where it is absolutely necessary, given the volume of the documentation required. Competent authorities should also indicate to the CSD prior to the start of the authorisation filing which language should be used for the application.

Q16: What are your views on the proposed draft RTS on CSD review and evaluation (Chapter III of Annex II) and draft ITS (Chapter II of Annex VI)?

This question refers to:
Section 3.2 of the Consultation Paper (p.44-46)
Annex 2 Chap. 3 (p.177-183): draft RTS
Annex 6 Chap. 2 (p.261-263): draft ITS

- **Access to data by the competent authority (art.38 RTS, p.177)**

ECSDA believes that requiring CSDs to provide a self-assessment against the CSDR requirements as part of the annual review, as suggested by art.38(1) of the draft RTS, would be very burdensome and disproportionate given that no such requirement is placed on other regulated entities such as CCPs, banks or investment firms.

We thus recommend amending art.38(1) as follows:

Article 38 - Access to data by the competent authority
1. For the purpose of the review and evaluation as referred to in Article 22(7) of Regulation (EU) No 909/2014, a CSD shall provide the information as defined in this chapter ***~~together with a self-assessment on the CSD's activities overall compliance with the provisions of Regulation (EU) No 909/2014 during the review period~~****, and any other information as requested by the competent authority.*

- **Documents that have been materially modified (art.40 RTS, p.177)**

ECSDA suggests adding the word "*materially*" in art.40 of the draft RTS to ensure consistency with the title of the article:

Article 40 - Documents submitted in the application for authorisation that have been materially modified
A CSD shall provide all documents submitted to the competent authority in the application for authorisation which have been ***materially*** *modified in the review period.*

- **Information relating to periodic events (art.41 RTS, p.178-179)**

ECSDA recommends adding "*where relevant*" at the end of the first sentence of art.41 of the draft RTS in order to give more flexibility to competent authorities as regards the list of documents they truly need in relation to periodic events.

As regards art.41(1)(e) and (f), ECSDA believes that it is not realistic to expect CSDs to provide information about "*potential*" litigation and that the draft RTS should be limited to actual litigation procedures.

As regards art.41(1)(h), we note the absence of a definition of what constitutes a "*complaint*". Given the high number of participants - let alone account holders in CSDs operating in direct holding markets - and issuers with which a CSD interacts on a daily basis, ECSDA recommends limiting art.41(1)(h) to formal complaints, i.e. complaints recorded and handled through the established procedures of the CSD, or alternatively requesting the CSD to report the number of complaints, rather than actually sharing details about all complaints received.

As regards art.41(1)(j), (k) and (t), the notion of materiality must be introduced. For art.41(1)(k), we suggest removing the word "*any*" to make it clear that CSDs should report only those operational incidents which have had an impact on the smooth functioning of core services.

As regards art.41(1)(m), we believe that the obligation imposed on CSDs should be limited to giving information on the incorporation of new types of conflicts in the register of conflicts of interest, given that there is little value in reporting conflicts of interest when these were identified, raised and managed in accordance with the CSD's policies.

As regards art.41(1)(n), we believe that a reference to conflicts of interest is confusing and unnecessary, given that these are covered by point (m).

As regards art.41(1)(r), ECSDA is not certain what is meant by "*business operations report*", especially because the term is not defined. We would thus welcome some clarifications, as well as the addition of the word "*relevant*" in order to ensure that such reports are only provided where meaningful and appropriate.

Art.41(1)(u) requires a CSD to provide *"information to any changes to the resolution plan"* to its competent authority as part of the annual review. As mentioned in our answer to question 15 (comments on art.5(5) of the draft RTS), we believe that the current formulation in the draft RTS is misleading. Unlike recovery plans, which are drafted and maintained by CSDs, resolution plans are the responsibility of resolution authorities. If ESMA's intention is to ensure that CSDs provide all the information necessary for the resolution authority to update the CSD's resolution plan, art.41(1)(u) should be reformulated accordingly and should include a reference to the resolution authority.

ECSDA thus recommends the following amendment to art.41 of the draft RTS:

Article 41 - Information relating to periodic events

1. For each review and evaluation, the CSD shall provide to the competent authority, ***where relevant****:*

[…] (e) information on any pending judicial, administrative, arbitration or any other litigation proceedings, particularly as regards tax and insolvency matters, that the CSD ~~***may be***~~ ***is*** *party to, and which may incur significant financial or reputational costs;*

(f) information on any pending judicial, administrative, arbitration or any other litigation proceedings, irrespective of their type, that a member of the management body or a member of the senior management ~~***may be***~~ ***is*** *party to and that may have an adverse impact upon the CSD;*

[…] (h) information on any ***formal*** *complaints received by the CSD in the review period, specifying the nature of the complaint, the handling of the complaint and date when the complaint was resolved;*

[…] (j) information on any ***material*** *changes affecting any links of the CSD, including the mechanisms and procedures used for settlement;*

[…] (k) information on ~~***any***~~ *operational incidents that occurred in the review period and affected the smooth functioning of any core services provided;*

[…] (m) information on ~~***all***~~ ***new*** *cases of identified conflicts of interest that occurred in the review period, including the way in which they were managed;*

(n) information on measures taken to address the identified technical incidents ~~***and conflicts of interest***~~ *as well as the results thereof;*

[…] (r) ***relevant*** *business operations report concerning the review period;*

[…] (t) information on any ***material*** *changes to the recovery plan, including the identification of the CSD's critical services, results of stress scenarios and recovery triggers, as well as the CSD recovery tools.*

[…] ~~***(u) information on any changes to the resolution plan established and maintained for the CSD so as to ensure continuity of at least its core functions, having regard to the size, systemic importance, nature, scale and complexity of the activities of the CSD concerned, and any relevant resolution plan established in accordance with Directive 2014/59/EU;***~~

(u) any information deemed necessary to ensure that the resolution plan established and maintained by the resolution authority ensures the continuity of at least the CSD core functions, having regard to the size, systemic importance, nature, scale and complexity of the activities of the CSD concerned, including any relevant resolution plan established in accordance with Directive 2014/59/EU;

- **Statistical data (art.42 RTS, p.180-181)**

ECSDA is concerned that some of the statistical data ESMA proposes to collect as part of art.42 of the draft RTS is inconsistent with the existing methodology used to report statistical data to central banks and, in some cases, goes beyond what is necessary to assess compliance with the CSDR.

EU CSDs already report statistical data to ESCB central banks on an annual basis (for each calendar year), using the so-called "Blue book" methodology. We understand that the statistical data described by ESMA in art.42 of the draft RTS would be of a different nature, i.e. intended for the competent authority, and not necessarily for public disclosure.

While we recognise the legitimate request of regulators to obtain more detailed statistical data than what is made publicly available, we believe that the underlying methodology for collecting settlement and other information on CSD activities should be identical in both cases ("Blue book" statistics reported to central banks and statistical data provided to competent authorities as part of the annual supervisory review). This would not only avoid placing a disproportionate burden on CSDs, but it would also facilitate the comparability of data and allow ESMA to aggregate the information transmitted by national competent authorities, if applicable.

In particular, we have identified issues with the following data items:

- ***Art.42(1)(b)***

ECSDA wonders whether the use of the term "*maintained*", in the context of this article, should be understood as meaning "*offered for settlement by a CSD*". We believe that ESMA needs to clarify the meaning of this term throughout the RTS, as explained in our answer to question 30.

If ESMA's intention is to obtain a list of ISIN codes under this heading, it should be aware that the list will amount to hundreds of thousands of ISINs for some CSDs.

Importantly, ECSDA would also like to stress that CSDs will often not have access to information on the country of incorporation of the issuer.

- ***Art.42(1)(c), (d) and (e)***

There is not always a market value available, especially for private issues (many of which are settled and held at CSDs in some European markets). Conversely, some instruments do not have a meaningful "nominal value" (e.g. listed equities), and so CSDs should only be expected to provide market or nominal values where these are available.

Moreover, ECSDA does not understand why the country of incorporation of participants or issuers is considered relevant by ESMA for supervisory purposes. As explained in our response to question 6 of the ESMA Consultation paper on draft Technical Advice on the CSDR, ECSDA does not think that the country of incorporation of a participant is an adequate proxy for the country of establishment of ultimate investors. There are many cases, today, of CSD participants holding securities on behalf of investors established in an (EU or non-EU) country different from the one where the participant itself is established, sometimes to a very large extent. Given that CSD participants are always wholesale financial institutions, and given that many of them operate in multiple markets, including outside the EU, we do not believe that there are supervisory concerns in relation to their use of a non-domestic CSD.

As regards issuers, CSDs often do not have information on the place of incorporation of the issuer, and in fact we believe that this information is not always relevant (especially in relation to debt instruments, investment funds, and non-equities in general). The law applicable to the issues admitted for settlement in a CSD, on the other hand, is important as it determines the rights and obligations of investors, as well as the services to be performed by the CSD.

- ***Art.42(1)(f)***

ECSDA would like to stress that CSDs currently do not have access to information on buy-ins and that collecting such data will involve very practical challenges, which are further detailed in our response to questions 7 and 23 of the Consultation Paper.

ECSDA recommends the following amendments to art.42 of the draft RTS:

Article 42 - Statistical data to be delivered for each review and evaluation

*1. For the purpose of the review and evaluation, the CSD shall provide the following statistical data to the competent authority covering the review period, **if and when applicable**:*

[No changes to (a)]

(b) a list of ~~***issuers and a list of***~~ *securities issues* ~~***maintained***~~ ***settled*** *by the CSD, including information on* ~~***the issuers' country of incorporation, highlighting***~~ *those* ***securities*** *for* ***which*** ~~***whom***~~ *the CSD provides notary services;*

(c) ***where available,*** *nominal* ~~***and***~~ ***or*** *market value of the securities maintained in each securities settlement system operated by the CSD in total and divided as follows:*

(i) by asset class (as specified in point d) of Article 4(2) of Regulation (EU) No … [RTS on settlement discipline]);

~~***(ii) by country of incorporation of the participant;***~~

~~***(iii)by country of incorporation of the issuer;***~~

(d) ***where available,*** *nominal* ~~***and***~~ ***or*** *market value of the securities centrally maintained in each securities settlement system operated by the CSD, divided as follows:*

(i) by asset class;

~~***(ii) by country of incorporation of the participant;***~~

~~***(iii)by country of incorporation of the issuer.***~~

(e) ***where available,*** *number, nominal value and market value of settlement instructions settled in each securities settlement system operated by the CSD in total and divided as follows:*

(i) by asset class;

~~***(ii) by country of the incorporation of the participant;***~~

~~***(iii) by country of incorporation of the issuer;***~~

[…]

Q17: What are your views on the proposed draft ITS on cooperation arrangements as included in Chapter III of Annex VI?

This question refers to:
Section 3.3 of the Consultation Paper (p.47-48)
Annex 6 Chap. 3 (p.263-267): draft ITS, including Annex 3 (Tables 1 to 4, p.294-300)

ECSDA has decided not to comment on question 17 since it pertains to communication among authorities.

Q18: What are your views on the proposed draft RTS on CSD recognition (Chapter IV of Annex II)?

This question refers to:
Section 3.4 of the Consultation Paper (p.49-50)
Annex 2 Chap. 4 (p.183): draft RTS

ECSDA agrees with the draft RTS on CSD recognition.

Q19: What are your views on the proposed approach regarding the determination of the most relevant currencies?

This question refers to:

Section 3.5 of the Consultation Paper (p.51)
Annex 2 Chap. 5 (p.184): draft RTS

ECSDA agrees with the proposed approach regarding the determination of the most relevant currencies. In case a CSD established in a country where the euro is not the official currency exceeds the 5% threshold for EUR, we wonder whether the draft RTS should specify that the ECB, rather than all central banks of the Eurosystem, should be considered as "*relevant authority*".

Q20: What are your views on the proposed draft RTS on banking type of ancillary services (Chapter VI of Annex II) and draft ITS on banking type of ancillary services (Chapter IV of Annex VI)?

This question refers to:
Section 3.6 of the Consultation Paper (p.52-53)
Annex 2 Chap. 6 (p.184-189): draft RTS
Annex 6 Chap. 4 (p.267-269): draft ITS, including Annex 2 (p.193-199)

It should be possible for CSDs that request an authorisation to perform banking-type ancillary services to submit a single authorisation file for both CSD and banking-type activities at the same time.

In line with our response to question 15, ECSDA believes that art.50(1)(g) of the draft RTS should be amended to reflect the fact that resolution plans, unlike recovery plans, are drafted and maintained by resolution authorities.

As regards art.50(3)(m)(v), we believe that the text should refer to article 30 rather than article 31 of the CSDR.

As regards art.50(h)(iii)(d), we find the current wording rather unclear and suggest aligning the terminology with that of the Level 1 CSDR text as much as possible.

ECSDA recommends amending art.50 of the draft RTS as follows:

Article 50 - Authorisation to provide banking-type ancillary services
1. A CSD shall ensure its application for the authorisation referred to in point (a) of Article 54(2) of Regulation (EU) No 909/2014 contains at least the following information […]
(g) ***~~the resolution plan established in accordance with Directive 2014/59/EU;~~****a programme of operations which as a minimum: […]*
3. An application for authorisation of a CSD referred to in point (b) of Article 54(2) of Regulation (EU) No 909/2014 shall contain at least the following information […]
(m) detailed information concerning the structural organisation of the relations between the CSD and the designated credit institution, including in particular information concerning:
*[…] (v) the service level agreement establishing the details of functions to be outsourced by the CSD to the designated credit institution or from the designated credit institution to the CSD and any evidence that demonstrates compliance with the outsourcing requirements set out in Article 3****~~0~~1*** *of Regulation (EU) No 909/2014;*

B. CSD requirements

Q21: What are your views on the proposed draft RTS on CSD participations (Chapter II of Annex III)?

This question refers to:
Section 4.1 of the Consultation Paper (p.54-57)
Annex 3 Chap. 2 (p.204-205): draft RTS

- **Definitions (art.1 RTS, p.203-204)**

Before commenting on the other chapters of the draft RTS, ECSDA would like to make some remarks on the definitions being proposed by ESMA under art.1 of the draft RTS.

First, ECSDA believes that the proposed definition of "*issuer CSD*" is incorrect (for example it would exclude CSDs which do not provide the notary service even though they might have links with other CSDs). It is also unnecessary, since it introduces potential ambiguities and confusion with the notion of "*central maintenance*", which is used in many other instances throughout the draft RTS. As explained more in detail in our response to question 30, we believe that for consistency purposes, the draft RTS should rely on the notion of "*central maintenance*" introduced by the Level 1 Regulation and should not introduce a different concept that could cause interpretation issues.

Second, the proposed definition of "*double-entry accounting*", being restricted to securities accounts, appears too narrow. CSDs perform double-entry accounting but such accounting does not always involve two securities accounts. For example, when external parties are involved, a CSD might make an entry to an internal nostro-type account that is mirroring the entry made by the third party in its own books. This distinction is very important in view of art.14 to 16 of the draft RTS on reconciliation.

ECSDA thus recommends amending art.1 of the draft RTS as follows:

*Article 1 – Definition**s***
For the purposes of this Regulation, the following definitions shall apply:
~~(a) 'issuer CSD' means a CSD which provides the core service referred to in point 1 of Section A of the Annex to Regulation (EU) No 909/2014 for a securities issue.~~
[no changes to (b)]
*(c) 'double-entry accounting' means that for each credit entry made on a**n** **~~securities~~** account maintained by the CSD, there is a corresponding debit entry on another **~~securities~~** account maintained by the CSD.*

- **CSD participations (art.2 RTS, p.204-205)**

ECSDA believes that the restrictions imposed on CSD participations by art.2 of the draft RTS (p. 204-205) are very stringent and will require some CSDs to restructure some of their existing participations, but we recognise important improvements compared to the measures initially envisaged in the ESMA Discussion Paper of March 2014.

Given that situations that require recovery and resolution are subject to significant elements of uncertainty and discretion, we recommend adding the phrase *"to the extent known or reasonably foreseeable"* in art.2(1)(b)(iii).

As regards art.2(1)(c), it should be clearly stated that the list of services provided in art.2(1)(c)(i), (ii) and (iii) is not exhaustive and that other services might be considered as complementary to a CSD's core and ancillary services. Indeed, according to art.18(4) of the CSDR, one of the criteria to be taken into account by competent authorities when deciding whether to authorise participations of CSDs in legal persons other than those providing the services listed in Sections A and B of the Annex is the extent to which the services provided by the other legal person are complementary to the services provided by the CSD. ECSDA believes that ESMA's attempt to translate this criterion into a list of entities (e.g. CCPs, trading venues and trade repositories) is not aligned with and results in too narrow an interpretation of art.18(4) of the CSDR, since it focuses on types of entities rather than on the nature of the services provided. We recommend an alternative approach whereby the draft RTS would provide examples of complementary services, as part of a non-exhaustive list, and taking into account the fact that all "*complementary services*" should contribute to enhance the safety, efficiency and transparency of financial markets, in line with the first sentence of Section B of the Annex of the CSDR.

Besides, we would like ESMA to confirm that art.2(1)(c) does not prevent a CSD from having a participation in an entity that serves several CSDs, not only the CSD that has the participation.

We recommend that art.2(1) of the draft RTS be amended as follows:

Article 2 - Criteria for the participations of a CSD

1. A CSD may have a new or keep an existing participation only in a legal person other than those providing the services listed in Sections A and B of the Annex of Regulation (EU) No 909/2014 if each of the following conditions is fulfilled:

[..] (b) the CSD fully capitalises, through financial resources that fulfil the criteria as set under Article 46 of Regulation (EU) No 909/2014, the risks resulting from any:

[…] (iii) loss sharing agreements or recovery or resolution mechanism of the legal person in which a CSD intends to participate ***to the extent known or reasonably foreseeable****.*

(c) the entity in which the CSD holds a participation is providing complementary services related to the core or ancillary services offered by ~~***the***~~ ***a*** *CSD,* ***understood as services that contribute to enhancing the safety, efficiency and transparency of the financial markets,*** *including* ***for instance~~, services offered by~~****: […]*

(i) organised trade execution and arranging of trades,

(ii) provision of clearing,

(iii) collection and maintenance of data.

~~*(i) central counterparties (CCPs) authorised or recognised under Regulation (EU) No 648/2012 (EMIR);*~~
~~*(ii) regulated markets and MTFs subject to Directive 2004/39/EC (MiFID); or*~~
~~*(iii)trade repositories registered or recognised under Regulation (EU) No 648/2012 (EMIR).*~~

Q22: What are your views on the proposed draft RTS on CSD risk monitoring tools (Chapter III of Annex III)?

This question refers to:
Section 4.2 of the Consultation Paper (p.58-59)
Annex 3 Chap. 3 (p.205-212): draft RTS

- **Governance arrangements (art.3 RTS, p.205-206)**

ECSDA welcomes art.3 of the draft RTS which recognises that the functions of Chief Risk Officer, Compliance Officer and Chief Technology Officer can be performed by a member of staff having other responsibilities as well, as long as potential conflicts of interest are managed appropriately. We believe that this approach is proportionate and will allow CSDs to ensure that these key functions are performed by qualified individuals in an optimal way.

However, as regards art.3(4), ECSDA is not convinced that imposing that the functions of Chief Compliance Officer and Chief Risk Officer be performed by different individuals is necessary. Although this will be the case in many firms, there are compelling reasons for CSDs to decide to entrust both functions to the same individual. Indeed, non-compliance is perceived as a major source of risk for today's financial institutions, and there are important synergies between the risk management function and the compliance function. These synergies have been discussed and described in various press articles and reports in recent years, with many experts expressing the view that compliance should be an integral part of risk management, and that the functions would thus benefit from being combined into a single individual[4].

ECSDA thinks that there is no reason to believe that having a single individual acting as CCO (Chief Compliance Officer) and CRO (Chief Risk Officer) could endanger the performance of the compliance and risk management functions. In fact, Directive 2006/73/EC (MiFID Implementing Directive), which regulates the compliance function in investment firms, states: *"The fact that risk management and compliance functions are performed by the same person does not necessarily jeopardise the independent functioning of each function."* Similarly, the 2005 report of the Basel Committee on Banking Supervision on "Compliance and the compliance function in banks" states that "*some banks may wish*

[4] See for instance:
http://blogs.reuters.com/financial-regulatory-forum/2012/04/05/time-to-merge-risk-management-and-compliance/ ,
http://download.pwc.com/ie/pubs/2014-pwc-ireland-compliance-operational-risk-management.pdf ,
http://iia.nl/SiteFiles/IIA%20NL%20Combining%20functions%202014.pdf and http://www.post-tradeviews.com/integrating-compliance-risk-management-functions-way-forward/

to organise their compliance function within their operational risk function, as there is a close relationship between compliance risk and certain aspects of operational risk."[5]

As a result, ECSDA recommends amending art.3(4) to allow the Chief Risk Officer and Chief Compliance Officer functions to be performed by the same individual, thereby allowing CSDs, if they so wish, to reap the efficiencies related to the integration of the compliance and risk management functions, while avoiding any inconsistencies with the legislation applying to banks:

Article 3 - Governance arrangements
4. A CSD shall establish lines of responsibility which are clear, consistent and well-documented. A CSD shall ensure that the functions of the chief risk officer, chief compliance officer and chief technology officer are carried out by different individuals, who shall be employees of the CSD or an entity within the same group. ***By way of exception, the functions of chief risk office and chief compliance officer might be performed by the same individual, provided this is approved by the CSD competent authority****. A single individual shall have the responsibility for each of these functions, without prejudice of the appropriate arrangements to mitigate over-reliance on individual employees. These individuals may undertake other duties outside the scope of the risk, compliance or technology functions provided that these do not have an operational or commercial nature and specific procedures are adopted in the governance arrangements to identify and manage any kind of conflict of interest that may arise.*

- **Risk management and internal control mechanisms (art.4 RTS, p.207-208)**

ECSDA supports the spirit of art.4(1) of the draft RTS and recognises the need for CSDs to assess the risks that their participants, as well as their participants' clients, pose to the CSD, in line with Principle 19 of the PFMI. That said, ESMA should keep in mind that CSDs do not incur risks from the clients of their participants and have no way of exercising any control over these clients, including in direct holding markets. We do not think that a legally binding text should impose unreasonable regulatory expectations onto CSDs, especially given that CSDs could be sanctioned for non-compliance with these requirements. We thus recommend removing the phrase *"and, where relevant, their clients"* from art.4(1).

Similarly, we are concerned that the current wording of art.4(2) would make CSDs legally responsible for assessing the risks they pose to other entities. Introducing such a requirement in Level 2 legislation would impose duties on CSDs without ensuring that they can access the required information to fulfil those duties, and is thus problematic. We thus suggest restricting the legal requirement to those risks to which the CSD itself is exposed.

As for art.4(9), we believe that the requirement to share *"rules, procedures and contractual arrangements"* with participants and even participants' clients is excessive and that it will give rise to a whole set of data protection and competition concerns. Participants' contractual documentation should

[5] See http://www.bis.org/publ/bcbs113.pdf

include all the information on the rights and obligation of participation in the CSD, and so there is no need for this additional requirement. As for clients of CSD participants, they only have a contractual relationship with a CSD participant. Requiring a CSD to share with a participant's client the details of a contractual arrangement the CSD has with the participant would very likely create competition concerns and violate contractual commitments and data protection rules.

Article 4 - Risk management and internal control mechanisms

1. A CSD shall have a sound framework for the comprehensive management of all relevant risks to which it is or may be exposed. A CSD shall establish documented policies, procedures and systems that identify, measure, monitor and manage such risks. In establishing risk-management policies, procedures and systems, a CSD shall structure them in such a way as to ensure that participants ~~***and, where relevant, their clients***~~ *properly manage and contain the risks they pose to the CSD.*

2. A CSD shall take an integrated and comprehensive view of all relevant risks. These shall include the risks it bears from ~~***and poses***~~ *to any other entities, including its participants and, to the extent practicable, their clients, as well as linked CSDs and central counterparties, trading venues, payment systems, settlement banks, liquidity providers and investors.*

[…] 9. The rules, procedures and contractual arrangements of the CSD shall be recorded in writing or on a durable medium. These rules, procedures, and contractual arrangements and any accompanying material shall be accurate, up-to-date and readily available to the competent authority~~***, participants, if affecting participants' rights and obligations and, where known by the CSD and where affecting clients' rights and obligations, their clients***~~*.*

- **Organisational structure (art.5 RTS, p.208-209)**

As regards art.5(5) of the draft RTS on the composition of CSD risk committees, ECSDA would like ESMA to clarify the meaning of the phrase *"where there are management body members sitting as members of the risk committee".* Our current understanding is that:

- A CSD risk committee is not necessarily composed of members of the management body, although it advises the management body;
- A CSD risk committee can be composed of executive managers, with the exception of the function of Chairman of the risk committee, which should be held by someone independent from the management of the CSD;
- The requirement to have a majority of non-executive members in the CSD risk committee only applies when the risk committee is composed of members of the management body.

We would welcome a confirmation that this understanding is correct. In particular, in the absence of a definition of the term "*non-executive member*" (both in the draft RTS and the Level 1 Regulation), we believe it would be helpful for art.5(5) of the draft RTS to clarify whether "*non-executive members*" means members of the management body which are not part of the senior management of the CSD, or whether it also includes CSD employees which are not part of the senior management.

We also recommend replacing the term "*recognised*" by "*relevant*" in art.5(5) of the draft RTS as follows:

Article 5 - Organisational structure

[…] 5. A CSD shall establish a risk committee that shall be responsible for advising the management body on the CSD's overall current and future risk tolerance and strategy. It shall be chaired by a person with ***relevant*** ~~***a recognised***~~ *experience on risk management and that is independent of the CSD's executive management. It shall be composed of a majority of non-executive members, where there are management body members sitting as members of the risk committee. It shall have a clear and public mandate and procedures and access to external expert advice where it may find fit.*

- **Conflicts of interest (art.6 RTS, p.209-211)**

ECSDA believes that the phrase "*larger group*" in the first sentence of art.6(1) of the draft RTS is unclear and thus recommends removing the word "*larger*", in line with article 26(7) of the CSDR.

As regards art.6(3)(a), we recommend including a definition of "*any person directly or indirectly linked to them*", distinguishing between legal and natural persons.

Similarly, the notion of "*connected person*" in art.6(3)(b) should be defined.

ECSDA suggests amending art.6 of the draft RTS as follows:

Article 6 - Conflicts of interest

[…] 1. Where a CSD is part of a ~~***larger***~~ *group, it shall place particular emphasis on the clarity of its governance arrangements, […]*

[…] 3. Such circumstances of potential conflicts of interest may include the following:

(a) where the CSD, any member of staff of the CSD, or any person directly or indirectly linked to them:

*[…] (b) where the members of the management body or senior management of the CSD have an indirect conflict with other connected persons****, as defined below:***

"Any person directly or indirectly linked to them" and "connected person" means:

- when referring to a legal person: directly or indirectly linked to the legal person by control;

- when referring to a natural person: the immediate family, being understood as the spouse or legal partner, family members in direct ascending or descending line and their spouses or legal partners, the siblings and their spouse or legal partners, and any person living under the same roof as the employees, managers or members of the management body.

Q23: What are your views on the proposed draft RTS on CSD record keeping (Chapter IV of Annex III) and draft ITS on CSD record keeping (Annex VII)?

This question refers to:

Section 4.3 of the Consultation Paper (p.60-64)
Annex 3 Chap. 4 (p.212-218): draft RTS
Annex 7 (p.306-322): draft ITS

ECSDA generally welcomes ESMA's approach on recordkeeping and believes that the requirements contained in the draft RTS are generally more workable than the proposals made in the ESMA Discussion Paper of March 2014.

We especially welcome:
- ESMA's decision to remove fields SR3, SR4, SR13 and SR14 proposed in the Discussion Paper and agreement that fields FR3 and FR9 (information on the client of participants) should be made optional, i.e. that records should only be maintained when CSDs have access to such information;
- ESMA's decision not to mandate an online inquiry possibility, query function through numerous search keys, and direct data feeds for regulators;
- The fact that CSDs can be allowed to store their records in proprietary format as long as the format can be converted without undue delay into an open format for regulatory reporting purposes.

ECSDA is nevertheless convinced that the draft standards on record keeping must be further recalibrated and that ESMA should:

(a) allow CSDs to keep their records in the current format and, if a certain format is mandated in the technical standards for the purpose of regulatory reporting, ensure that this format is compatible with global ISO standards;
(b) only require CSDs to maintain those records that they need to provide services;
(c) not confuse CSD records with the type of data that CSDs need to maintain to resume activities in case of operational problems as part of their business continuity policy;
(d) refrain from imposing the record keeping requirements in a retro-active way, so that only records maintained by CSDs after they have been authorised under the CSDR - and after the record keeping requirements have entered into effect - are assessed against the new requirements;
(e) foresee a phased-in implementation for record keeping requirements, in line with the phase-in for settlement discipline measures, i.e. ideally for a period of at least 24 months after the ESMA technical standards enter into force. Such phase-in should apply at a minimum for those records linked to settlement discipline information and to the use of LEIs for reporting purposes.

- **Compatibility with global ISO standards**

We are concerned that some of the codes being proposed by ESMA are not compatible with current ISO standards, going against the spirit of article 35 of the CSDR and potentially hampering ongoing and future efforts at harmonising global market and messaging standards on transaction types. CSDs and their participants operate in global financial markets and compatibility with open and internationally-recognised standards must be ensured when creating new transaction and status codes, even if these are only used in Europe on a mandatory basis.

Discussions with other market participants, messaging providers and regulators have revealed that the following ESMA proposals are currently not aligned with ISO standards:

Consultation Paper	***Codes not aligned with ISO***
Transaction types: - Draft RTS: Art.9(2)(c) - Draft ITS: Table 1, row 2	TRAO (OTC purchase or sale of securities)
	COLL (collateral management)
	CUST (custody related operations)
	CCPC (CCP-cleared transactions related to late settlement penalties)
Status types: - Draft RTS: Art.9(2)(v) - Draft ITS: Table 1, row 21	MATY (matched settlement instructions that are not settled)
	MATN (settlement instructions that are not matched)
	HOLD (settlement instructions on hold)
	PART (partially settled settlement instructions)
	FAIL (failed settlement instructions)
	RECL (recycled settlement instructions)
	DELL (cancelled settlement instructions)
	SETL (settled settlement instructions
Information on buy-ins: - Draft RTS: Art.9(2)(w) - Draft ITS: Table 1, row 22	Buy-in initiated: Y/N
	Length of extension period: 2 digits
	Length of deferral period: 2 digits
	Length of the buy-in period: 2 digits
	Buy-in successful: Y/N
	Payment of cash compensation: Y/N

ECSDA thus suggests that new codes should only be introduced following discussions with international standard-setters with a view to ensure that the new European standards are fully compatible with global market practice going forward.

Furthermore, the following considerations should also be taken into account by ESMA when finalising the draft standards:

- As explained in our response to question 4, there is currently no agreed harmonised market practice in the EU on how to populate the transaction type field (i.e. which value to assign for the different types of transactions). Compatibility with ISO alone is not sufficient and ensuring that the codes are used correctly by all market players takes time.
- ECSDA wonders which operations ESMA intends to cover under "*custody related operations*", and to what extent these would differ from "*corporate actions*". Since such a distinction is currently not commonplace, we would have welcomed further explanations in the Consultation Paper.
- Since a settlement instructions can have multiple statuses at once (e.g. matched and on hold), the presentation of the fields should be adjusted to clarify which statuses are cumulative and which ones are mutually exclusive.
- ESMA should avoid introducing unnecessary codes such as "*recycled*". As explained in our response to question 5, there is no such code today and yet it is possible to control whether an instruction has been recycled (e.g. if it is still pending the next business day). We understand that ESMA wishes to ensure that competent authorities can assess whether a CSD complies with the

CSDR technical standards requiring instructions to be recycled, but we believe that such control can be made by deduction, i.e. without needing a separate code.

- ESMA should also be aware that there are many securities for which CSDs maintain no holdings. In order to avoid an inflation of unnecessary records, ESMA should consider excluding such securities from the list of records to be maintained, since most of the fields would anyways remain empty.

- **The use of LEIs to identify issuers**

Many issuers are not financial institutions and are thus not entitled to obtain a BIC. By requiring CSDs to report either a BIC or an LEI for issuers as part of their recordkeeping requirements, the draft RTS creates the following problems:

(1) Neither the Level 1 text of the CSDR nor the draft RTS being proposed by ESMA impose obligations on issuers. The draft standards require CSDs to provide such information (a BIC or an LEI for each issuer for which they have issues on deposit), but it is impossible for a CSD to force an issuer to obtain such identification information. There is thus a serious enforcement problem.

(2) The enforcement problem is further aggravated in the case of non-EU issuers (especially frequent for debt instruments and investment funds held at European CSDs). How can such issuers be required to obtain an LEI by an EU Regulation on CSDs?

(3) ESMA should not underestimate the scale and complexity of transitioning tens of thousands of European issuers (of all sizes and types, for all asset classes) to the LEI. The cost for collecting and maintaining issuer LEIs will be very high for CSDs since they will typically have many more issuers than they have participants. The complexity would be further exacerbated if LEIs are requested retrospectively for all issues already under circulation. Even if LEIs are eventually adopted by European issuers, the process will take time and is very unlikely to fit in the timeframe of CSD authorisations under the CSDR.

Given these major challenges, ECSDA believes that imposing the use of LEIs for issuers is not practically possible in the context of the CSDR. If EU law-makers wish to encourage or mandate the adoption of LEIs by issuers in the future, this should be done outside the scope of the CSDR and keeping in mind practical constraints as regards non-EU issuers.

- **The use of LEIs to identify CSD participants**

ECSDA welcomes ESMA's approach allowing CSDs to use BICs in their day-to-day processing. However, in order to provide LEIs for the purpose of regulatory reporting, CSDs will have to develop and maintain system functionalities to allow for the conversion of processing data using BICs to reporting data using LEIs. Such functionalities will be costly and complex to develop.

In particular, given that a single BIC will sometimes correspond to multiple LEIs, and conversely an LEI might be linked to more than one BIC, the conversion mechanism will often require, not just a list of BIC and LEI codes, but also CSDs' own client identifiers (proprietary codes). Taking such constraints into account as well as the fact that not all CSD participants have yet obtained an LEI, ECSDA suggests that CSDs should be allowed by ESMA to continue to use BICs in their regulatory reports during an appropriate transition phase of at least 24 months.

- **Identifiers for accountholders in direct holding markets**

Field 17 in Table 2 of the annex to the draft ITS (p.314) requires CSDs to keep records, where available, on "*securities account holders*", either using an LEI or a BIC (for legal persons) or a 50 alphanumerical digits national identifier (for natural persons).
ECSDA believes that these requirements, which are only relevant for CSDs operating in direct holding markets, should be amended to take into account the requirements of these markets.

For natural persons, CSDs recognise the need to maintain full records of account holders, including a national identifier which, depending on the country, will contain a different number of alphanumerical digits. We thus understand the "*50 alphanumerical digits*" mentioned in the draft ITS to be a maximum, and we expect ESMA to recognise the national identifiers currently used by CSDs to identify natural persons who are account holders.

For legal persons, the requirement to use a BIC or an LEI will be problematic, given that many businesses recorded as account holders in CSDs are not banks (and thus do not have a BIC) and cannot be forced by the CSD to obtain an LEI. These legal persons include small brokers, asset managers, and even non-financial firms which hold securities on their own account. Such legal persons are typically identified by CSDs using a business ID or other similar identifier. As in the case of issuers, we foresee significant enforcement problems if CSDs are required to record LEIs for such entities, since the CSD Regulation does not impose obligations on these entities and CSDs have no means to impose the acquisition of an LEI by these legal persons, especially in a retro-active way.

We thus recommend amending field 17 of Table 2 of the Annex as follows:

17	*Identifiers of participants and of other securities account holders*	***For CSD participants,*** *ISO 17442 Legal Entity Identifier (LEI) 20 alphanumerical character code, or Bank Identifier Code (BIC) (with the obligation to convert to LEI for reporting purposes to authorities)* *For* ***account holders which are*** *legal persons,* ***business identifier or other equivalent identifier***

		***For account holders which are natural persons**, available national identifier **~~for natural persons~~** (**up to a maximum of** 50 alphanumerical digits) which allows the unique identification of the natural person at a national level*

- **Recordkeeping and disaster recovery (art.8 RTS, p.212-213)**

ECSDA generally agrees with article 8 and the general requirements it contains as regards recordkeeping by CSDs. However we disagree with the reference made to business continuity in art.8(1) of the draft RTS, and we believe that such reference should be removed.
Indeed, as specified in the Level 1 CSDR, the purpose of recordkeeping is to *"enable the competent authority to monitor the compliance with the requirements under this Regulation."* (art.29 of the CSDR). This objective is fundamentally different from business continuity planning, which is covered under separate articles of the Regulation. The legal records kept under the draft RTS have to be maintained by CSDs for 10 years and cannot be expected to be used as "back-ups" to reconstruct instructions and resume operations in case of a technical failure or other incident. The recovery of business following an interruption of service is an entirely different process which is part of Business Continuity Planning (of which disaster recovery is a subset) and is monitored by competent authorities as part of operational risk management by the CSD. To avoid such unnecessary confusion between legal records and business continuity planning, we suggest removing the reference to "*business continuity purposes*" in art.8(1).

As regards art.8(8), ECSDA does not believe that technical standards should include a requirement for CSDs to provide direct data feeds to their competent authority upon request. A direct data feed is not necessary to demonstrate that a CSD's compliance with the CSDR and it entails considerable costs, while potentially raising confidentiality issues in relation to participants' activity in the CSD. Given that competent authorities can obtain information promptly from the CSD upon request, we suggest deleting art.8(8).

ECSDA suggest amending art.8 of the draft RTS as follows:

Article 8 - General Requirements
1. A CSD shall maintain full and accurate records of all its activities. Such records shall be readily accessible~~, including for business continuity purposes,~~ and shall include the records specified in this Regulation.
[…] ~~8. A CSD shall provide the competent authority with a direct data feed to transactions, settlement instructions, and position records, when requested by the competent authority, provided that the CSD is given sufficient time to implement the necessary facility to respond to such a request.~~

- **Records on buy-ins (art.9 RTS, p.213-215)**

ECSDA believes that art.9(1) of the draft RTS imposes excessive requirements onto CSDs, and confuses CSD records with the type of data that CSDs store for business continuity purposes (and which can be used to conduct a comprehensive and accurate reconstruction of each operation). Indeed, it is not realistic to expect each and every CSD to maintain records of *"all transactions, settlement instructions and settlement restriction orders it processes"* for 10 years. Such a requirement is not necessary to ensure compliance with the CSDR and ECSDA thus suggests its deletion.

As regards art.9(2), ECSDA believes that some of the requirements are too prescriptive and that CSDs should rather be expected to maintain the information they receive as part of client instructions, including relevant timestamps. For instance, points (p) and (q) should be rephrased to clarify that the information should be kept in CSD records only if it is included as part of the settlement instructions received by the CSD.

Art.9(2)(w), on the other hand, should be deleted or amended based on the final requirements on buy-ins. Once more, ECSDA would like to reiterate the important practical difficulties CSDs will face to collect such information, as described in our answer to question 7 of the Consultation Paper.

We thus suggest the following amendments to art.9 of the draft RTS:

Article 9 - Transaction/Settlement Instruction (Flow) Records

~~1. A CSD shall keep records of all transactions, settlement instructions and settlement restriction orders it processes, and shall ensure that its records include all information necessary to conduct a comprehensive and accurate reconstruction of each operation.~~

2. In relation to every settlement instruction and settlement restriction order received, a CSD shall, immediately upon receiving the relevant information, make and keep updated a record of at least the following details, where applicable:

[…] (p) identifier of the participant's client, where ***it is included in the settlement instruction~~known to the CSD~~****;*

(q) identifier of the client of the participant's counterpart, where ***it is included in the settlement instruction~~known to the CSD~~****;*

~~(w) where a buy-in process is initiated for a transaction, the following details:~~

~~(i) length of extension period;~~

~~(ii) where applicable, length of the deferral period;~~

~~(iii)length of the buy-in period;~~

~~(iv) if the buy-in is successful or not; (v) other relevant information in accordance with Regulation (EU) No…[RTS on settlement discipline]~~

- **Position records (art.10 RTS, p.215-216)**

ECSDA believes that art.10(2) of the draft RTS, and in particular points (a), (f), (g), (h) and (i), should be interpreted flexibly, given that issuers are not always CSD clients. In fact, an issuer is sometimes not

even aware that its securities have been admitted to a CSD because it uses an agent which acts as the CSD client and manages the recording of the issue(s) on its behalf. CSDs should thus only be expected to maintain such records when information is available to them.

As for art.10(3), ECSDA does not believe that point (b) is appropriate, since CSDs often cannot distinguish whether a participant account is an "own account", an omnibus or an individually segregated account. It is the use which a participant makes of a securities account which determines the category, and in many cases the CSD has no knowledge of the way a participant uses its securities account(s). The definitions of "*omnibus client segregation*" and "*individual client segregation*" in art.38 of the CSDR do not require CSD participants to inform the CSD about which accounts are "*omnibus accounts*" and which accounts are "*segregated*" accounts. It only requires CSDs to offer the possibility for participants to maintain multiple accounts, some of which will include securities held on behalf of multiple clients.

Since art.10(3)(b) of the draft RTS is not practically implementable by most CSDs (at least in indirect holding markets), ECSDA suggest deleting it:

Article 10 - Position (Stock) Records
[…] 3. At the end of each business day a CSD shall make a record in relation to each position including the following details, to the extent they are relevant for the position:
[…] ***~~(b) type of securities accounts (i.e. if it is an own account, omnibus account, individual account, other);~~***

- **Business records (art.12 RTS, p.217-218)**

ECSDA suggests amending art.12(2) of the draft RTS as follows to add more clarity to the requirements under points (o) and (r):

Article 12 - Business Records
[…] 2. The records referred to in paragraph 1 shall be made each time a material change in the relevant documents occurs and shall include at least:
*[…] (o) written communications with the competent authority, ESMA and relevant authorities****, in relation to the CSD's obligations under Regulation (EU) 909/2014****;*
[…] (r) the relevant documents describing the development of ***new services by the CSD~~business initiatives~~****;*

- **Format of records (art.1 ITS, p.307-308)**

ECSDA recommends amending art.1 of the draft ITS as follows:

Article 1 - Format of records

1. A CSD shall retain the records specified in Article 9 of Regulation (EU) No… [RTS on CSD requirements], adopted pursuant to Article 29(3) of Regulation (EU) No 909/2014, for all transactions, settlement instructions and settlement restriction orders it processes, ***where available,*** *in the format set out in Table 1 in the Annex.*

2. A CSD shall retain the records specified in Article 10 of Regulation (EU) No… [RTS on CSD requirements], adopted pursuant to Article 29(3) of Regulation (EU) No 909/2014, for the positions corresponding to all the securities accounts it maintains, ***where available,*** *in the format set out in Table 2 in the Annex.*

3. A CSD shall retain the records specified in Article 11 Regulation (EU) No… [RTS on CSD requirements], adopted pursuant to Article 29(3) of Regulation (EU) No 909/2014, for the ancillary services it provides, ***where available,*** *in the format set out in Table 3 in the Annex.*

4. A CSD shall retain the records specified in Article 12 of Regulation (EU) No… [RTS on CSD requirements], adopted pursuant to Article 29(3) of Regulation (EU) No 909/2014, for activities related to its business and internal organisation, ***where available,*** *in the format set out in Table 4 in the Annex.*

5. ***For participant data, a~~A~~*** *CSD may use a proprietary format only if this format can be converted without undue delay into an open format for reporting purposes to authorities in accordance with Regulation (EU) No 909/2014.*

- **Timing of implementation for recordkeeping requirements**

Despite important improvements compared to the recordkeeping requirements initially suggested in the Discussion Paper of March 2014, ECSDA believes that the draft RTS on recordkeeping cannot be realistically implemented by the time CSDs obtain their authorisation, i.e. towards the of end 2016. This is especially due to the transaction and status codes being proposed by ESMA. Experience with the establishment of new codes shows that a lot of work is required not only to adapt IT systems of CSDs and their users, but also to ensure harmonised usage of these by all actors across EU markets. As an illustration, the ISO change management process takes between 1 and 2 years, and this does not include the subsequent work on market adoption, which is usually incremental.

Since many records are related to compliance with the settlement discipline rules of the CSDR, ECSDA strongly recommends that the timeline for implementing the draft technical standards on recordkeeping be aligned with the timeline for implementing the draft technical standards on settlement discipline. In other words, compliance with both sets of requirements should only be enforced after a transition period of at least 24 months following publication of the relevant technical standards.

Furthermore, CSDs should not be required to apply CSDR record keeping requirements retroactively. CSDs should start keeping records based on the Level 2 standards requirements as soon as these requirement come into effect. They should not have to modify the records for the 10 years prior to their authorisation and/or prior to the entry into force of the record keeping requirement. CSDs should be allowed to keep these 'older' records in the format applicable at the time as per local regulations.

Q24: What are your views on the types of records to be retained by CSDs in relation to ancillary services as included in the Annex to the draft RTS on CSD Requirements (Annex III)? Please provide examples regarding the formats of the records to be retained by CSDs in relation to ancillary services.

This question refers to:
Annex 3 Chap. 4, art.11 (p.217): draft RTS, including the Annex on "Ancillary Services Records" (p.236-239)

ECSDA agrees with ESMA that CSDs should keep standardised records for ancillary services. Nonetheless, the current formulation of art.11(1) of the draft RTS is too restrictive and does not take into account the fact that the information items contained in the Annex of the draft RTS will not always be available. For example, when CSDs provide securities lending and borrowing facilities to their participants as agent, they do not always offer collateral valuation services, and information on the collateral valuation is thus not always available to them. The "*purpose*" of each securities lending and borrowing operation is also typically only known by the participants, not the CSD.

As a result, more flexibility is needed to ensure that CSDs are actually able to comply with the record keeping requirements for ancillary services. In particular, removing the phrase "*at least*" from art.11(1) is indispensable to recognise the different depths of services offered by CSDs in each category of ancillary services. CSDs with a basic service offering will typically need to keep fewer records for a given ancillary service than CSDs having a more sophisticated offering for the same ancillary service category.

ECSDA thus recommends amending art.11(1) of the draft RTS as follows:

Article 11 - Ancillary Services Records
1. A CSD shall keep ***~~at least~~*** *the types of records specified under the Annex* ***where available for~~, depending on~~*** *each of the ancillary services provided by a CSD in accordance with Section B and C of the Annex to Regulation (EU) No 909/2014. […]*

Given the existing diversity in CSD business models and the fact that many CSDs will offer services which are not explicitly listed in Section B of the Annex of the CSDR, ECSDA believes that the list of records to be kept by each CSD authorised to operate in the EU should be agreed with the competent authority, using the Annex of the draft RTS as a basis, but allowing for the list of records to be customised based on the specific types of services provided by the CSD.

ESMA should also be aware that, in some cases, CSDs might keep records which relate to both core and ancillary services. Although most of the time records will be different for core and ancillary services, there might be cases where the records cannot easily be segregated, e.g. in relation to ancillary services related to the settlement service, such as matching and routing. To avoid duplicate records and unnecessary complexity, ECSDA believes that the possibility for CSDs to maintain records covering both core and ancillary services should be acknowledged by ESMA as long as:

- The necessary information on ancillary services can be retrieved from the records (e.g. in the case of matching, from the audit trail of the settlement instruction);
- Segregation of core and ancillary services in enforced for analytical accounting, billing, statistical purposes etc.

Q25: What are your views on the proposed draft RTS on reconciliation measures included in Chapter V of Annex III?

This question refers to:
Section 4.4 of the Consultation Paper (p.65-68)
Annex 3 Chap. 5 (p.219-221)

ECSDA is convinced of the importance of solid reconciliation procedures and supports the overall aim of Chapter V of the draft RTS. Nonetheless, we disagree with some important aspects of the draft RTS and believe that amendments are necessary to avoid unintended consequences.

- **General reconciliation measures (art.14 RTS, p. 219)**

As mentioned in our response to question 16, the use of the term "*maintained*" throughout the RTS is confusing. Given that reconciliation via CSD links is covered separately under article 48(6) of the CSDR and under the draft RTS on access and links, ECSDA recommends using the term "*centrally maintained*" in article 14(1), for consistency purposes (see our response to question 30 for further details):

Article 14 – General reconciliation measures
1. A CSD shall perform the verification measures referred to in Article 37(1) of Regulation (EU) No 909/2014 for each securities issue ***centrally*** *maintained by the CSD.*
The CSD shall also compare the previous end-of-day balance with all the settlements made during the day and the current end-of-day balance for each securities issue maintained by the CSD.

- **Reconciliation problems (art.17 p.221)**

Suspension of settlement should not be automatically triggered in case of minor reconciliation discrepancies, e.g. when a small amount of securities appears to have been unduly "created" or "deleted".

Art.17(2) of the draft RTS (p.221 of the Consultation Paper) states that: *"Where the reconciliation process reveals an undue creation or deletion of securities, the CSD shall suspend the securities issue for settlement until the undue creation or deletion of securities has been remedied."*

ECSDA agrees with the spirit of art.17 but believes that this particular paragraph could have negative consequences for financial stability and should be redrafted to avoid creating unnecessary systemic risk. Indeed, a suspension of settlement might be appropriate to reduce risk in cases of major reconciliation problems, e.g. if many securities holders are affected, or if a few securities holders are affected in a substantial way. However, suspending all settlement in a share might in some instances

be excessive and counterproductive, i.e. if the securities unduly "created" or "deleted" only represent a very small fraction of a total issue and/or only affect very few securities holders.

Although most reconciliation issues can be expected to be solved before the start of the next business day, in rare cases investigations might take more time and, in such a scenario, the damage caused by the suspension of the settlement in a whole securities issue (in terms of fails, loss of market confidence, reputational damage for the issuer…) could be greater that than resulting uncertainty from letting the reconciliation issue unsolved for a few days.

A suspension of settlement could have the following systemic consequences, for instance:

- a CCP does not receive the relevant security as collateral;
- a bank using the security to receive central bank liquidity does not have access to the liquidity when required;
- trading in the securities continues whereby settlement obligations build up;
- settlement fails generate settlement penalties and a buy-in is executed.

ESMA should also be aware that suspending settlement in a financial instrument is likely to have consequences beyond the CSD and up to the trading level.

ECSDA thus suggests a reformulation of art.17(2) of the draft RTS as follows:

Article 17 - Problems related to reconciliation

[…] ***2.*** *Where the reconciliation process reveals an undue creation or deletion of securities, the CSD* ***~~shall~~ may*** *suspend the securities issue for settlement until the undue creation or deletion of securities has been remedied.*

In the event of suspension of the settlement referred to in the first subparagraph, the CSD shall inform without undue delay its participants and its competent authority and relevant authorities.

Q26: Do you believe that the proposed reconciliation measures where other entities are involved in the reconciliation process for a certain securities issue within the meaning of Article 37(2) of CSDR are adequate? Please explain if you think that any of the proposed measures would not be applicable in the case of a specific entity. Please provide examples of any additional measures that would be relevant in the case of specific entities.

- **Reconciliation with other entities (art.16 RTS, p. 220-221)**

ECSDA is concerned that art.6 of the draft RTS will be impossible to implement unless its scope is adjusted. Indeed, the current drafting of the article covers different scenarios which are fundamentally different and must be distinguished.

These scenarios are:

- **Scenario 1: The CSD provides notary services for the securities**, meaning that securities are initially entered into the CSD in book-entry form.
- **Scenario 2: The CSD provides central maintenance services for the securities, but not the notary service.** As per art.3 of the CSDR, securities have to be recorded in book-entry form in a CSD where those securities are traded on a trading venue (article 3 does not require the "initial" recording or notary function to take place in a CSD). In this case, the notary service is performed by another entity but there is a close relationship with the CSD. In general, there is a one-to-one relationship between the CSD and the provider of notary services (except for eurobonds, with a two-to-one relationship between the 2 ICSDs and the common depositary).
- **Scenario 3**: **The CSD holds securities through a CSD link.**
- **Scenario 4: The CSD is a mere intermediary: it does not provide central maintenance or notary services for this instrument, and it does not hold the securities via a CSD link.** This scenario is typical for certain international funds kept by transfer agents.

Understanding the different implications of each scenario is very important, and we believe that only scenario 2 should fall under the scope of art.16 of the draft RTS, both for legal and practical reasons.

Scenario 1 allows for internal reconciliation within the CSD between the total number of securities on the issuance account and the total number of securities on participants' accounts. No "*other entities*" being involved, art.16 of the draft RTS does not need to apply.

Scenario 2, like Scenario 1, is covered under art.37 of the CSDR. However, because the notary service is not provided by the CSD but by an external party, art.16 of the draft RTS applies. Reconciliation requires comparing the total number of securities on the issuance account at the external provider of notary service and the total number of securities held on participants' accounts at the CSD.

Scenario 3, on the other hand, is covered by article 48 of the CSDR, and is thus elaborated further in the draft RTS on access and links (article 6). Covering this scenario under the draft RTS on reconciliation measures would create unnecessary overlaps between different technical standards and would not follow the mandates under Level 1.

Scenario 4, finally, is not covered by the Level 1 CSDR, since the EU legislator deliberately decided not to include fund transfer agents in the scope of the CSDR requirements.

Including scenario 4 (and 3) in the draft RTS is thus inconsistent and, most importantly, it would not be feasible because:

- Unlike in scenarios 1 and 2, in scenario 4 (and 3), the CSD is not involved in the verification of the integrity of the issue; the CSD "reconciles" with the external notary as any other intermediary;
- Such reconciliation might be less frequent than daily, depending on the service level offered by the entity that provides notary services. CSDs have no authority to impose daily reconciliation on these entities, which are not subject to the CSDR requirements;

- Unlike in scenarios 1 and 2, a reconciliation difference at a CSD in scenario 4 (and 3) would not compromise the integrity of issue;
- Unlike in scenarios 1 and 2, in scenario 4 (and 3) the CSD (investor CSD in scenario 3) is not empowered to initiate a suspension of settlement in case of reconciliation problems.

ECSDA thus believes that art.16(1) of the draft RTS should be amended as follows:

Article 16 - Other entities involved in the reconciliation process
1. Where other entities are involved in the reconciliation process for a certain securities issue within the meaning of Article 37(2) of Regulation (EU) No 909/2014 ***and where the CSD provides the central maintenance service for that issue****, the measures to be taken by the CSD and those other entities to ensure the integrity of the issue shall include at least: […]*

Furthermore, ECSDA is worried that art.16(5) of the draft RTS could cause severe difficulties for CSDs operating in direct holding markets. Indeed, it will often not be technically possible for those CSDs to provide information to *"other holders of securities accounts"* on a daily basis given the lack of direct communication channel and the fact that such information is typically provided to account holders by account operators. We also do not think that it is necessarily practical for account operators to provide daily reconciliation information to account holders.

In order to ensure an equal treatment of CSDs operating in direct and indirect holding markets, we recommend the following amendments to art.16(5) of the draft RTS:

Article 16 - Other entities involved in the reconciliation process
[…] 5. The participants ~~***and other holders of securities accounts maintained by***~~ ***of*** *a CSD shall be entitled to receive at least the following information specified for each securities account and for each securities issue on a daily basis:*
[…] ~~***Where applicable, a CSD shall require the account operators to provide the information referred to in the first subparagraph to the holders of securities accounts maintained by the CSD.***~~

Q27: What are your views on the proposed reconciliation measures for corporate actions under Article 15 of the draft RTS included in Chapter V of Annex III?

- **Reconciliation measures for corporate actions (art.15 RTS, p.219-220)**

Corporate actions are initiated by issuers and processed by CSDs. ECSDA thus suggests the following reformulation of art.15(1) of the draft RTS:

Article 15 - Reconciliation measures for corporate actions that would change the balance of securities accounts maintained by the CSD

*1. A CSD shall not **~~initiate the~~** process**~~ing of~~** a corporate action that would change the balance of securities accounts maintained by the CSD until the reconciliation measures specified under Article 14 and, where applicable, under points a) and b) of Article 16(1) are completed at the end of settlement on the respective business day.*

Q28: What are your views on the proposed draft RTS on CSD operational risks included in Chapter VI of Annex III?

This question refers to:
Section 4.5 of the Consultation Paper (p.69-72)
Annex 3 Chap.6 (p.222-231)

- **Operational risks posed by service providers (art.20 RTS, p.222-223)**

In line with our answer to question 15 and our comments on the definition of outsourcing, we believe that it is important to restrict the scope of art.20 of the draft RTS to critical service providers on which CSDs rely for the continuous operation of core services. CSDs should indeed be expected to identify those utilities and service providers towards which they have a "critical" dependence, i.e. providers that perform, on a continuing basis, activities essential to the operation of CSD core services. Such providers might include for instance IT or standard messaging providers whose services are critical for the processing and settlement of instructions and the failure of which might impair CSDs' ability to meet regulatory requirements on the continued provision of a core service. Focusing on critical providers and dependencies affecting the provision of core services is consistent with the approach adopted in the PFMI and the CPMI-IOSCO assessment methodology for expectations on critical service providers. It would ensure that services which are not directly related to the operation of a CSD such as basic telecommunication services, water, electricity and gas are out of scope.

ECSDA thus recommends amending art.20 of the draft RTS as follows:

Article 20 - Operational risks that may be posed by utilities and service providers
*1. A CSD shall identify **critical** utilities providers and **critical** service providers based on its dependency on them **for the continuous operation of its core services**.*
*2. A CSD shall take appropriate actions to manage the **critical** dependencies referred to in paragraph 1 through adequate contractual and organisational arrangements as well as specific provisions in its business continuity policy and disaster recovery plan, even before any relationships are made operational with such providers.*
*3. A CSD shall ensure that its contractual arrangements with **~~any~~critical** providers identified under paragraph 1 require the CSD's approval before the critical service provider can itself outsource material elements of the service provided to the CSD, and that in the event of such arrangement, the level of service and its resilience is not impacted, as well as full access to the necessary information is preserved.*
*4. The outsourcing CSD shall establish clear lines of communication with the **critical** providers referred to in paragraph 1 to facilitate the flow of information in both ordinary and exceptional circumstances.*
*5. A CSD shall inform its competent authority about **~~any~~critical** dependencies on **critical** utilities and service providers and take measures to ensure that authorities may obtain information about the performance of such **critical** providers, either directly or through the CSD.*

- **Article 27 (p.226-227) on IT tools**

ECSDA believes that annual IT audits are only appropriate for the main IT systems linked to the provision of core services by a CSD, and we thus suggest amending art.27(11) accordingly. Other IT systems that are not of critical importance for the functioning of the CSD should be reviewed periodically, but the appropriate timeframe for the respective system should be left up to each CSD to determine.

We recommend amending art.27(11) of the draft RTS as follows:

Article 27 – IT tools
[…] 11. The IT systems and the information security framework ***in relation to the CSD core services*** *shall be reviewed, at a minimum, on an annual basis. They shall be subject to independent audit assessments and the results of these assessments shall be reported to the management body and shall be made available to the competent authority.*

ESMA should be aware that internal IT audits by CSDs will not be allowed on the TARGET2-Securities platform of the Eurosystem, and that only external examinations by an examiner appointed by the Governing Council will be possible.

- **Articles 28 to 33 (p.228-231) on business continuity**

ECSDA generally supports ESMA's approach in Section 4 of the draft RTS on business continuity. That said, we do not understand why the timeframe for disaster recovery should be fundamentally different in the case of a cyber-attack than in the case of a terrorist attack or a pandemic situation, for instance. In the case of the 11 September 2001 terrorist attacks in the United States, the banks operating from New York's Twin Towers took between 36 and 48 hours to resume operations. We believe that CSDs will always do their best to resume operations as soon as possible, and that the two hours recovery-time contained in the PFMI and the CSDR Level 1 is a helpful benchmark, but regulators must also recognise that exceptional crises might be of such scale that the benchmark cannot be met, irrespective of the cause (whether a cyber-attack or another event).

ECSDA thus suggests amending art.30(2) as follows:

Article 30 - Business Continuity and Disaster Recovery plans
[…] 2. The requirement under point c) of paragraph 1 shall not apply in the case of ~~***cyber-attacks***~~ ***exceptionally severe events.***
In ***such cases*** ~~***the case of a cyber-attack***~~*, a CSD shall assess the nature of the problem and shall determine an appropriate recovery time for the CSD's critical functions in order to minimise the damage caused by the adversarial actions.*

The CSD's critical functions shall be resumed within maximum 12 hours, unless this would jeopardize the integrity of the securities issues or the confidentiality of the data maintained by the CSD.

As regards art.33 of the draft RTS, ECSDA believes that requiring a CSD to notify its competent authority of each and every test performed in the context of operational risks is excessive and could potentially result in more than a hundred notifications each year per CSD, only a few of which might be truly meaningful from the point of view of the supervisor. Examples of insignificant tests from a supervisory point of view include new office software deployment for staff, routine test of the alarms systems etc. Moreover, without prejudice to the obligation for CSDs to perform tests with the frequency required by the business continuity policy, we expect the results of the tests to be communicated annually to competent authorities as part of the supervisory review.

Besides, since art.33 only refers to Section 4 of Chapter VI of the RTS on business continuity, the word "*chapter*" should be replaced with the word "*section*".

We recommend that art.33 of the draft RTS be reformulated to leave some flexibility for the CSD not to notify routine or insignificant tests to the competent authority:

Article 33 – Duty to notify
A CSD shall promptly notify the competent authority of the results of any ***substantial*** *tests performed in the context of this* ***section*** ~~***chapter***~~.

Q29: What are your views on the proposed draft RTS on CSD investment policy (Chapter VII of Annex III)?

This question refers to:
Section 4.6 of the Consultation Paper (p.73-75)
Annex 3 Chap. 7 (p.232-235): draft RTS

- **Articles 34 to 37 (p.232-235) on investment policy**

First, ECSDA recommends that government debt referred to in art.34(1)(a)(i) should explicitly include local and regional governments, central banks and supranational public authorities.

Second, ECSDA believes that art.34(1)(c) is too restrictive and that the average time-to-maturity of a CSD's portfolio could be extended to 5 years, with the maximum time-to-maturity no longer than 11 years. For instruments with minimal market or credit risk, there is no correlation between their liquidity and time-to-maturity. For instance, securities issued by governments and central banks are generally highly liquid, regardless of whether their time-to-maturity is 1, 2, 5 or 10 years. Currently, 10-year Treasury Bonds are commonly used by governments for managing their public debt, so their liquidity is high and a risk analysis is available. This is why art.114 of Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms states that *"exposures to Member States'*

central governments, and central banks denominated and funded in the domestic currency of that central government and central bank shall be assigned a risk weight of 0 %, regardless of their time-to-maturity".

In fact, portfolio diversification including instruments with longer time-to-maturity can be more beneficial for CSDs than a concentration of positions exclusively on short-term instruments. This is especially true in the current low rate environment for the euro currency where a 2-year time-to-maturity restriction would force some CSDs to invest in instruments with a negative yield, thereby eroding their capital.

Third, ECSDA believes that art.34(2) should be redrafted to allow CSDs to use interest rate derivatives to hedge interest rate risk and thus reduce their exposure to interest rate risk.

ECSDA thus recommends the following amendments to art.34 of the draft RTS:

Article 34 - Highly liquid instruments with minimal market and credit risk
1. Financial instruments can be considered highly liquid financial instruments, bearing minimal credit and market risk under Article 46 of Regulation (EU) No 909/2014 if they are debt instruments meeting each of the following conditions:
(a) they are issued or explicitly guaranteed by:
(i) a ***local or national*** *government;*
[…] (c) the average time-to-maturity of the CSD's portfolio does not exceed ~~***two***~~ ***five*** *years,* ***and no single investment has a time-to-maturity superior to eleven years****;*
[…] 2. Derivative contracts can also be considered highly liquid financial investments, bearing minimal credit and market risk if they are entered into for the ***following*** *purpose****s:*** ~~***of***~~
(i) *hedging currency risk arising from the settlement in more than one currency in the securities settlement system operated by the CSD****;***
(ii) hedging interest rate risk in relation to the CSD's investment book*.*

As regards art.35(3) and (5), ECSDA considers the proposed investment restrictions too conservative given that CSDs, unlike CCPs, do not guarantee the performance of settlement with their own assets. We believe that there is no reason to require CSDs to have immediate access to the assets invested and to liquidate them on the next business day and we think that a 3-day liquidation period would be more appropriate. CSDs typically plan their liquidity needs taking into account current and projected liabilities and should be able to manage them using this 3-day period. Even in extreme situations, such as the liquidation of the CSD's activities, there is no need to have access to all the assets within a day.

We thus recommend amending art.35 of the draft RTS as follows:

Article 35 - Appropriate timeframe for access to assets
[…] 3. A CSD that holds cash assets shall be able to have ~~***immediate***~~***swift*** *and unconditional access to those cash assets and take all appropriate measures for that purpose.*

[…] 5. Where a CSD holds the securities with an authorised credit institution, it shall hold them in an individually segregated account in the books of a CSD and be capable of accessing and liquidating them ***within three*** ~~***on the***~~ *business day****s from*** ~~***following***~~ *the day when****re*** ~~***re***~~ *a decision to liquidate the assets is taken.*

We also think that ESMA should consider lifting some restrictions in relation to the capital held in excess of minimum capital requirements, i.e. allowing CSDs to invest this part of their capital in equities, corporate bonds, and instruments with a longer maturity, in order to support diversification.

As regards art.36 of the draft RTS on portfolio diversification, ECSDA agrees with the proposed wording. We would only like to point out that CSDs might decide to use their own infrastructure to keep their own assets, as this eliminates custody risk. The criterion of geographical diversification, while generally important, should not be used to force CSDs to increase their custody network when this results in more costs, risks and complexity.

C. Access and Links

The following questions refer to:
Section 5 of the Consultation Paper (p.76-92)
Annex 4 (p.240-253): draft RTS
Annex 8 (p.323-3337): draft ITS

Q30: What are your views on the proposed draft RTS on access (Chapters I-III of Annex IV) and draft ITS on access (Annex VIII)?

ECSDA believes that the proposed definitions of "*issuer CSD*" and "*investor CSD*" in article 1 of the draft RTS (p.242) are not necessary and actually create potential overlaps and confusion with the notions of "*maintenance*" and "*central maintenance*" used in many instances throughout the RTS. We also believe that the distinction between "issuer" and "investor" CSD was deliberately not introduced in the Level 1 text by the EU legislator as it is not a legal notion and presents some practical problems. The EU legislator, instead, introduced the term of "*central maintenance*", which is defined as *"providing and maintaining securities accounts at the top tier level"*. For consistency purposes and for ensuring clarity in implementation, ECSDA recommends that the draft RTS rely on the notion of central maintenance introduced by the Level 1 CSDR and do not introduce a different concept which could cause interpretation issues.

In order to achieve ESMA's aims, we also recommend the use of the terms "*centrally maintained*" whenever possible rather than the mere use of "*maintained*". The term "*non-centrally maintained*" is not defined in the CSDR and is therefore not a service a CSD would be authorised for. We thus recommend that ESMA should replace the term by referring to Section B(3) of the Annex of the CSDR, i.e. *"establishing CSD links, providing, maintaining and operating securities accounts" which covers situations whereby the CSD does not act as provider of "central maintenance".*

ECSDA recommends that art.1(c) and (d) of the draft RTS be deleted as follows:

Article 1 – Definitions […]
~~(c)'issuer CSD' means a CSD which provides the core service referred to in point 1 of Section A of the Annex to Regulation (EU) No 909/2014 for a securities issue.~~
~~(d) 'investor CSD' means a CSD which has a link with an issuer CSD either directly or via an intermediary allowing its participants to hold securities in its securities settlement system which were issued through the issuer CSD.~~

- **Article 2 (p.242-245) on risks to be taken into account before establishing a link**

ECSDA generally agrees with art.2 of the draft RTS but remarks that, by covering CSD participants and linked financial market infrastructures at the same time, the article creates some apparent inconsistencies. For instance, art.2(6) seems to have been drafted mostly with CSD participants in mind, and it is sometimes difficult to imagine how the requirement can be applied to a trading venue with which a CSD has a link (trade feed), since the trading venue will not be a CSD participant and thus might not have any financial obligations towards the CSD.

Some confusion is also introduced by the fact that the article covers at the same time the CSD's risk assessment and the subsequent analysis by the competent authority in case the CSD has refused access to a participant, issuer, CSD or other financial market infrastructure and the requesting party has complained about this refusal. In order to avoid confusion regarding this sequence, ESMA should consider separating the different responsibilities in art.2 of the draft RTS more clearly.

We would like ESMA to confirm that non-EU participants in EU CSDs:

- will not be required to be supervised under an equivalent regulatory regime as that of the home Member State of the CSD. While CSD participants should, as a rule, always be supervised institutions, the regulatory regime applicable to them will often not be comparable with that applying in the EU;
- will be subject to the Settlement Finality Directive (SFD) as participants in EU CSDs, without that this would require the jurisdiction in which they are established to enforce the SFD.

ECSDA thus recommends amending art.2(2)(b) of the draft RTS as follows:

Article 2 - Risks to be taken into account by CSDs and competent authorities […]
2. When assessing the legal risks following a request for access by a requesting participant, a CSD and its competent authority shall take into account at least the following criteria:
[…] (b) In the case of a requesting party established in a third country, the requesting party is not subject to a ***legally sound*** *regulatory and supervisory framework* ***~~comparable to that of the home Member State of the CSD~~****, and the rules of the CSD concerning settlement finality referred to in Article 39 of Regulation (EU) No 909/2014 are not enforceable* ***~~in the jurisdiction~~ in case of a failure*** *of the requesting party;*

Q31: What are your views on the proposed draft RTS on CSD links as included in Chapter IV of Annex IV?

- **Article 4 (p.248-249) on conditions for "adequate protection"**

First, ECSDA fears that the proposed drafting of art.4(1)(e) of the draft RTS is too restrictive and might result in the termination of many links maintained by EU CSDs with non-EU CSDs. Indeed, most non-EU CSDs do not offer a *"level of asset protection that has comparable effects to the one ensured by the regime applicable in the case of the securities settlement system operated by the requesting CSD".* This does not mean that these CSDs are "unsafe", but simply that their legal regime is not comparable to EU standards, which are among the strictest if not the strictest in the world. The overview of CSD links published by ECSDA on 26 January 2015[6] shows that European CSDs, including some small and medium-sized CSDs, have been maintaining links with non-EU CSDs for many years, for the benefit of their market participants, and we are not aware that these links are a particular source of concern for regulators.

We fully recognise the need for due diligence and legal opinions, as mentioned in art.4(1)(e) of the draft RTS, but we believe that the phrase *"comparable effects"* could de facto prevent existing links (e.g. with CSDs in Japan, South Korea, Canada, the US, Australia, to name just a few) to be maintained by EU CSDs, since the applicable legal regimes in the non-EU jurisdictions might not qualify as having *"comparable effects"*.

ESMA should be aware that CSD links are an alternative to accessing a CSD through an intermediary such as a custodian bank, an arrangement which is not subject to the same strict rules. Imposing excessively burdensome requirements on CSD links will reduce the number of links and the level of activity through CSD links, going against the public policy objective of a more integrated post trade infrastructure. Such an outcome would not result in more safety for cross-border settlement since transactions will have to take place outside the existing network of infrastructures.

Second, ECSDA disagrees with article 4(1)(f) and does not understand why ESMA wishes to prevent DvP links in commercial bank money, given that DvP links are on the contrary strongly encouraged by the CSDR. Today, many domestic CSDs operating without a banking licence maintain DvP links with the ICSDs, for instance, and we are not aware that such links are a cause of concern for regulators. In fact, the current practice at some (I)CSDs with a banking licence is to require participants, including CSDs acting as investor CSDs, to open a cash account in addition to a securities account at the (I)CSD in order to allow for commercial bank money settlement (e.g. when this is the only option). The current wording of article 4(1)(f) would de facto restrict all links to ICSDs and CSDs with a banking licence to FoP links, removing all the efficiencies related to DvP settlement in foreign currencies.

[6] See http://ecsda.eu/wp-content/uploads/2015_01_26_CSD_Links_Overview.pdf

Third, the "*emergency plan*" for links mentioned by ESMA in art.4(1)(h) should not be a standalone document and should form an integral part of the business continuity policies of the respective CSDs.

Fourth, ECSDA recommends amending art.4(1)(d) to exclude those elements of the link arrangement that are commercial (e.g. prices and fees) from the "*terms and conditions*" to be communicated to CSD participants.

Finally, as regards CSDs established in the EU, ECSDA would like ESMA to confirm that art.4(1)(b) allows a requesting CSD to rely on the receiving CSD's regulatory authorisation under the CSDR without being obliged to conduct a full risk assessment on the receiving CSD's financial soundness, governance arrangements, processing capacity, operational reliability and reliance on a critical service provider, and take measures to monitor and manage these risks.

ECSDA believes that art.4 of the draft RTS should be amended as follows:

Article 4 - Conditions for the adequate protection of linked CSDs and of their participants
1. A CSD link shall be established and maintained under the following conditions:
[…] (d) The requesting CSD shall make the ***operational*** *terms and conditions of the link arrangement available to its participants to enable the participants to assess and manage the risks involved.*
(e) Before the establishment of a link with a third country CSD, the requesting CSD shall perform an initial verification of the local legislation applicable to the receiving CSD. In performing such a verification, the CSD shall ensure that the securities maintained in the securities settlement system operated by the receiving CSD benefit from a ***legally sound*** *level of asset protection* ~~***that has comparable effects to the one ensured by the regime applicable in the case of the securities settlement system operated by the requesting CSD***~~*. The requesting CSD shall require legal opinions addressing at least the following issues:*
(i) the entitlement to the securities, including the law applicable to proprietary aspects, nature of the rights on the securities, permissibility of an attachment or freeze of the securities; and
(ii) the impact of insolvency proceedings on at least segregation, settlement finality, procedures and deadlines to claim the securities.
~~***(f) A requesting CSD that is not authorised to provide banking-type ancillary services in accordance with Article 53 of Regulation (EU) No 909/2014 shall not receive banking-type of ancillary services from a receiving CSD authorised to provide banking-type ancillary services in accordance with Article 53 of Regulation (EU) No 909/2014, in relation to the settlement of the cash leg to be processed through the link***~~
[No changes to (g)]
(h) The requesting CSD shall be responsible for having conducted end-to-end tests with the receiving CSD before the link becomes operational. An emergency plan shall be established ***as part of the business continuity plans of the respective CSDs*** *before the link becomes operational, covering at least the situation where the securities settlement systems of the linked CSDs malfunction or break down and the remedial actions in such events.*

- **CSD links via intermediaries (art.5 RTS, p.249-251)**

ECSDA does not support the approach taken by ESMA in art.5(1) which treats direct operated CSD links the same way as indirect links. Both the Level 1 CSDR and current oversight practices within the ESCB clearly distinguish between direct and indirect CSD links. Operated links are merely a subset of direct CSD links, and are treated as direct links for supervisory purposes. The role of the operator in managing the CSD's account at another CSD is not comparable to the role of the subcustodian holding securities on behalf of a CSD at another CSD, and the risk implications differ significantly. As a result, in order to ensure consistency with the Level 1 CSDR, we believe that art.5 of the draft RTS should be limited to indirect links, and should not apply to direct operated links.

Furthermore, ECSDA is concerned that some of the conditions imposed on indirect links by art.5 of the draft RTS are overly strict and will not be possible to fulfil for the many indirect links that EU CSDs currently maintain with third country CSDs. For example, third country intermediaries cannot always be expected to be compliant with rules *"at least as stringent as"* the those contained in the EU banking regulations, given that the EU has established one of the strictest regimes for intermediaries worldwide. The same is true for *"individual segregated accounts"*, which art.5(1)(h) would make compulsory for indirect links with non-EU CSDs. ECSDA assumes that the phrase *"at least an individually segregated account"* refers to the definition of individual client segregation in art.38(4) of the CSDR and would require that assets held by an investor CSD on behalf of its participants be held in a securities account distinct from securities accounts held on behalf of other entities than the investor CSD, without that the segregated account necessarily be opened in the name of the investor CSD. We would welcome a confirmation of this interpretation by ESMA given that, in some cases, a third country CSD might not offer individual segregated accounts, due either to restrictions in the national legal framework or to local market practices. ECSDA believes that such restrictions should not prevent EU CSDs from maintaining indirect links with non-EU CSDs, as long as the risks are managed by the CSD and considered appropriate by the CSD's supervisory authorities and overseers.

We thus recommend amending art.5 of the draft RTS as follows:

Article 5 - Risk monitoring and management when using indirect links ~~***or an intermediary to operate a CSD link***~~

1. Where a requesting CSD uses an indirect link ~~***or an intermediary to operate the link***~~*, it shall ensure that:*

(a) The intermediary is one of the following:

[…] (ii) a third country financial institution that is subject to and complies with prudential rules considered by the relevant competent authorities ~~***to be at least as stringent as those laid down in Regulation (EU) No 575/2013***~~ *and which has robust accounting practices, safekeeping procedures, and internal controls and that ensures the full segregation and protection of those securities, enables the requesting CSD's prompt access to the securities when required and that the requesting CSD can demonstrate to have low credit risk based upon an internal assessment by the requesting CSD. In performing such an assessment, the requesting CSD shall employ a defined and objective methodology that shall not fully rely on external opinions.*

[…] (c) The intermediary is able to ensure~~***, in accordance with the rules applicable in the home Member State of the requesting CSD,***~~ *the confidentiality of information provided through the intermediary in connection to the link. The requesting CSD shall perform the assessment based on the information provided by the intermediary, including on any legal opinions or any relevant legal arrangements.*

*[…](h) At least an individually segregated account at the receiving CSD is used for the operations of the link**, where the receiving CSD is established in the Union. In such cases, t**he requesting CSD shall ensure that it can access the securities held in the individually segregated account at any point in time, including in the event of a change or insolvency of the intermediary.*

- **Reconciliation of links (art.6 RTS, p.251-252)**

As in the case of art.4 and 5 of the draft RTS, ECSDA is concerned that the proposed requirements will not be practically implementable for links with non-EU CSDs. This is for instance the case with art.6(1)(a) of the draft RTS, which requires daily statements of opening and closing balances, as well as movements, something not all non-EU CSDs are currently able to provide.

As regards art.6(1)(b), the second sentence is unclear and introduces confusion between direct operated links and indirect links. We thus suggest removing this sentence, since the requirement contained in the first sentence is sufficient and covers all scenarios.

As regards art.6(2), ECSDA suggests removing the reference to "*common depositaries*" since this case is covered under art.16 of draft RTS on CSD requirements (p.220).

ECSDA strongly disagrees with art.6(3) of the draft RTS and believes it should be deleted. Indeed, only the issuer CSD can decide to suspend settlement as a result of an *"undue creation or deletion of securities"*. The investor CSD does not have access to the full picture and there is no reason why it should be treated differently from any other participant in the issuer CSD.

As regards art.6(4), ECSDA would like to express its support for the comments and drafting proposals contained in the T2S AG response to the ESMA Consultation, especially as regards the need to distinguish corporate actions on stock and on flows.

ECSDA recommends amending art.6 of the draft RTS as follows:

Article 6 - Reconciliation Methods for Linked CSDs

1. The reconciliation methods referred to in Article 48(6) of Regulation (EU) No 909/2014 shall include at least the following measures:

*(a) The receiving CSD shall transmit to the requesting CSD **~~daily~~ regular** statements of information specifying the following, per account number and per securities issue: […]*

(b) The requesting CSD shall conduct a daily comparison of the opening balance and the closing balance communicated to it by the receiving CSD or by the intermediary with the records maintained by the requesting CSD itself.

~~In the case of an indirect link, the daily statements referred to in point a) of the first subparagraph shall be transmitted through the intermediary that operates the link.~~

*2. **~~If a common depository or any other relevant entity is used by the~~ For** CSDs in an interoperable link, the CSDs shall reconcile their positions among themselves **~~and with that other entity~~** on a daily basis **as in (1)**.*

~~***3. Where the reconciliation process reveals an undue creation or deletion of securities, the linked CSDs shall suspend the securities issue for settlement until the undue creation or deletion of securities has been remedied.***~~

~~***The linked CSDs shall analyse the impact and, where considered necessary, shall harmonize any restrictions regarding the respective securities issue, involving also the intermediary in the case of indirect link.***~~

4. In the case of a corporate action that would change the balance of securities accounts held by a CSD with another CSD, ***and in respect of booked positions ("corporate actions on stocks"), the bookings of the corporate action movements*** ~~***settlement by the former CSD in the relevant securities issues***~~ ***in the books of the former CSD*** *shall not* ***be finalised*** ~~***commence***~~ *until the corporate action* ***movements relating to booked positions ("corporate actions on stocks") of the relevant securities issues have***~~***has***~~ *been fully processed* ***in the latter CSD.***

The issuer CSD shall ensure the transmission, ***to all its participants that are CSDs, or that are acting on behalf of CSDs*** ~~***including through its participants***~~*, of timely information on corporate actions processing****.*** ~~***to a***~~***All*** ~~***the***~~ *investor CSDs involved in the holding chain for a specific securities issue,* ~~***enabling the coordination of their actions with regard to the adequate reflection of the corporate actions in the securities settlement systems operated by the respective investor CSDs***~~ ***shall likewise ensure the transmission of timely information to all their participants that are CSDs, or that are acting on behalf of CSDs****.*

2. Responses to the ESMA consultation questions (technical advice)

Q5: Do you agree with the proposed frequency of one year for the assessment of the substantial importance of a CSD in another Member State?

Yes.

Q6: What are your views on the proposed indicators?

ECSDA has serious doubts about the validity of ESMA's indicators and remains convinced, in line with the approach taken in article 23 of the Level 1 CSDR, that the notion of "*provision of services*" should be limited to cases where the CSD has set up a branch in another Member State or provides notary and/or central maintenance services in that country, i.e. excluding the settlement service.

We thus disagree with Section 3.5 of the ESMA Consultation Paper on technical advice (p.22-24) and believe that the "settlement indicator" is not appropriate.

We believe that consistency with the Level 1 CSDR is all the more important since the text of art.24(4) of the CSDR approved by COREPER (Council representatives) prior to the finalisation of the text by lawyer-linguists clearly stated that, *"when taking into account the situation of the securities markets in the host Member State, the activities of a CSD that has established a branch have become of substantial importance for the functioning of the securities markets and the protection of the investors in that host Member State, the home and host competent and relevant authorities shall establish cooperation arrangements for the supervision of the activities of that CSD in the host Member State."* Despite the adoption of a different wording in the published text of the CSDR, we believe that the intention of the EU legislator was clearly to limit the cases of "systemic importance" to CSDs having a branch in a host Member State, and not to cover all other cases of cross-border service provision.

Irrespective of the consistency problem with the Level 1 text, ECSDA further strongly disagrees with ESMA's statement in paragraph 86 of the Consultation Paper (p.23-24) that *"participants of the host Member State would be an adequate proxy for investors".* There are many cases, today, of CSD participants holding securities on behalf of investors established in different (EU or non-EU) countries than the country where the participant itself is established, sometimes to a very large extent. Furthermore, in addition to be contradicted by today's reality in many CSDs, this statement goes against the primary objective of the CSDR and the EU Single Market, which is precisely to further encourage and facilitate the use by investors of intermediaries (CSD participants) established in a different EU jurisdiction than their own.

We recognise the difficulty of establishing a workable threshold in those cases where CSDs have no information on the country of establishment of their participant's clients, but we think that this limitation

should not be a reason to use an inaccurate and obsolete criterion that will not accommodate the natural evolution of the EU single market.

As a result, ECSDA thinks that the indicators included in Section 3.4 of the Consultation Paper as regards the central maintenance service (p.20-22) are not adequate and should be reviewed. The country of establishment of CSD participants is not a good indicator and it is perfectly possible for a foreign intermediary (CSD participant) to hold securities primarily for domestic end investors, and vice-versa to hold securities for investors which are established in foreign countries different from that where the participant is established. Since the criteria and thresholds to be defined by ESMA for determining "substantial importance" are meant to involve host authorities from a safety and investor protection perspective, the "nationality" of CSD participants is largely irrelevant since it might be totally different from that of the actual holders of the security.

Furthermore, we note that the proposed denominators for the thresholds' calculations will often not be available to the CSD, and that the relevant data but thus be collected by the competent authority. This is the case for:

- The nominal value of securities "non-centrally maintained" by all CSDs established in the EU;
- The nominal value of the FoP settlement instructions settled by all CSDs established in the EU;
- The nominal value of settlement instructions settled by all CSDs established in the EU from participants as well as for other holders of securities accounts of the host Member State.

ECSDA supports ESMA's decision not to include collateral management services in the assessment of the threshold for the "central maintenance service".

Finally, as regards Section 3.3 of the Consultation Paper on the notary service (p.19-20), ECSDA believes that the proposed indicators are more appropriate.

Q7: What are your views on the proposed thresholds?

ECSDA has no comments on the level of the proposed thresholds but we welcome ESMA's suggestion to undertake a simulation exercise before the draft technical advice is finalised in order to assess the number of authorities that would be required to establish cooperation arrangements as result of the proposed thresholds. ECSDA is currently collecting data from its members in support of the simulation exercise and we hope that the results will help achieve more workable criteria for determining the appropriate thresholds.

Q8: Do you believe that the proposed indicators and thresholds are relevant in the case of government bonds? If not, please provide details and arguments.

No comments.

3. Responses to the ESMA consultation questions (Guidelines)

Q1: What are your views on the proposed Guidelines?

ECSDA fully supports ESMA's proposal to publish guidelines to cover cases when a CSD requires access to a CCP or trading venue and we regret that the principles contained in the Guidelines cannot be incorporated into regulatory technical standards, due to constraints in the Level 1 CSDR. We believe this would have been more consistent.

As regards the statement, in paragraph 13(d), that: *"(d) Access should not create additional operational risks for the receiving party (…)"*, we believe that it would be preferable to refer to "*material operational risks*" to avoid that this criterion be interpreted too broadly to justify a refusal of access, given that the establishment of a link between a CSD and another market infrastructure necessarily entails some operational risks, although these can often be easily managed.

Although the proposed guidelines do not refer to the complaint procedure by art.53(3) of the CSDR, ECSDA remarks that the draft ITS on access will apply in case a CSD believes it is denied access on unfair grounds.