# Draft
# ECSDA CSDR
# Penalties Framework

03/07/2019

# DRAFT ECSDA SETTLEMENT FAILS PENALTIES FRAMEWORK

Contents

# GLOSSARY

| Acronym or abbreviation | Description |
|---|---|
| BD | Business day(s) |
| CA | Competent Authority(ies); relevant supervisor(s)/ regulator(s) of the CSD |
| Calculating CSD | CSD subject to CSDR where the actual settlement (fail) is taking place; the Calculating CSD will calculate, report and collect/ distribute penalties to its participants (that may as well be CSDs); in cross-CSD settlement fails scenarios involving direct links, to avoid duplication of penalties calculation and reconciliation issues between CSDs, penalties shall exclusively be calculated by the Calculating CSD. |
| CCP | Central Counterparty |
| CSD | Central Securities Depository |
| CSDR | Regulation (EU) no 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 ("EU CSD-Regulation"). Note that CSDR is applicable to both, CSDs and International Central Securities Depositories (ICSDs, i.e. Clearstream Banking Luxembourg or Euroclear Bank).

See https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014R0909

For the full package of related texts including standards and guidelines, see https://www.esma.europa.eu/regulation/post-trading/settlement |
| DR | EU Delegated Regulation. In the Framework, and unless specified otherwise, DR relates to penalty reference prices and applicable rates. See http://eur-lex.europa.eu/eli/reg_del/2017/389/oj |
| ECB | European Central Bank |
| ESMA | European Securities and Markets Authority |
| ISD | Intended Settlement Date; date on which the settlement instruction shall settle (same meaning as "Requested Settlement Date (RSD)") |
| LMFP | Late matching Fail Penalty; penalty that applies due to the matching taking place after the ISD. See also "SEFP". |
| MiFID II/ MiFIR | Markets in Financial Instrument Directive II; Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 |

| Acronym or abbreviation | Description |
|---|---|
| | http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065&from=EN<br><br>Markets in Financial Instrument Regulation; Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014<br><br>http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0600&from=en |
| RTS | Regulatory Technical Standard, which are endorsed by the European Commission by means of a delegated act supplementing an EU Regulation or a Directive |
| SDR | CSDR Settlement Discipline Regime; amongst others, prescribing CSD settlement functionalities, measures to prevent settlement fails (incl. penalties, mandatory buy-ins and sanctions to participants) and reporting to be provided. The standards describing the regime in detail can be found here:<br><br>https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2018.230.01.0001.01.ENG&toc=OJ:L:2018:230:TOC |
| SEFP | Settlement Fail Penalty; penalty that applies due to the non-settlement of a matched transaction on or after its ISD |
| SFD | EU Settlement Finality Directive; Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems<br><br>http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:1998:166:0045:0050:EN:PDF |
| SSR | Short Selling Regulation; Regulation (EU) No 236/2012 of the European Parliament and of the Council of 14 March 2012<br><br>http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32012R0236&from=EN |
| T2S | Target 2 Securities; European Central Bank (ECB) centralised settlement platform |
| T2S CSDR TF | Task Force composed of representatives from ECB, Central Banks, CSDs, ECSDA and the Banking community to discuss requirements towards and solutions of T2S related to CSDR |

# INTRODUCTION

On 23 July 2014, the European Parliament and the Council have issued Regulation (EU) No 909/2014 (later, CSDR[1]) aiming at the harmonisation of the regulatory environment of securities settlement and Central Securities Depositories in the Union.

On 13 September 2018, the European Commission officially published Delegated Regulation (DR) 2018/1229, supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on the settlement discipline regime (SDR)[2].

The introduction to the DR states:

"*One of the main objectives of the Regulation is to improve the safety and efficiency of securities settlement, in particular for cross-border transactions, by ensuring that buyers and sellers receive their securities and money on time and without risks. To achieve this objective, the Regulation harmonises the timing and framework for securities settlement in the Union. In particular, it provides for a set of measures to prevent and address failures in the settlement of securities transactions ('settlement fails'), commonly referred to as settlement discipline measures.*"

This ECSDA CSDR Settlement Fails Penalties Framework (later, "the Framework") is the effort of compliance with the Regulation and harmonisation of settlement penalties mechanisms across CSDs subject to CSDR or regulation alike and constitutes a **market practice** for the CSDs mentioned in Annex IV of the Framework.[3]

**The Framework solely focuses on the <u>settlement fails penalties</u>-related aspects of the CSDR settlement discipline regime.**

European CSDs also take into account the regulatory and contextual elements as described below and having led the CSDs to develop the present Framework:

(i.) The Framework recognises the importance of the provisions of CSDR Articles 6 & 7 (with regard to measures to prevent and to address settlement fails), as well as Delegated Regulation 2018/1229 detailing the Settlement Discipline Regime (later, SDR). The provisions aim at increasing settlement efficiency and harmonising settlement discipline measures across the Union through the following four key pillars:

Pillar I.    Measures to prevent settlement fails:

---

[1]  Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directive 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (OJ L 257, 28.8.2014, p. 1). The Regulation and delegated acts can be found here:
https://www.esma.europa.eu/regulation/post-trading/settlement
[2] Full text can be found here: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32018R1229
[3] The CSDs involved in drafting of the Framework include members of ECSDA subject to the CSDR or aiming at compliance with equivalent legislation, as well as NBB-SSS (the National Bank of Belgium Securities Settlement System) and BOGS (the Bank of Greece Securities Settlement System). Full list of CSDs using the Framework as a market practices can be found in Annex IV.

- Trade allocations and confirmations (obligation for Investment Firms, not applicable to CSDs);

- Automation of CSDs´ settlement processes and reporting of "manual interventions";

- Settlement instructions mandatory matching fields;

- CSDs´ settlement functionalities aiming at preventing settlement fails (e.g. bilateral cancellation, hold & release, partial settlement) and possible derogation from the requirements to offer partial settlement and hold & release functionalities by CSDs under certain conditions.

Pillar II.   Requirements to monitor and report settlement fails:

- CSDs are required to monitor and analyse settlement fails and CSD participants´ settlement efficiency, including setting up working groups to define measures to improve efficiency;

- Settlement efficiency/ fails reporting to authorities, CCPs/ Trading Venues and public.

Pillar III.   Requirements for CSDs to charge cash penalties to users that cause settlement fails (sole subject of this ECSDA Penalties Framework):

- For matched settlement instructions failing to settle on the Intended Settlement Date (ISD), a daily calculation, (at least) monthly collection, distribution and reporting of penalties to CSD participants are required to be developed by CSDs subject to CSDR or alike regulation.

Pillar IV.   Rules requiring a mandatory buy-in:

- Trading parties and CCPs are required to initiate a mandatory buy-in after a specific period of time after the ISD (CSD role is limited to information gathering and regulatory reporting).

(ii.)   The CSDR SDR RTS foresee an implementation on 14 September 2020[4].

(iii.)   Pursuant to delegated acts, any relevant additional ESMA clarification (once officially published) will be taken into account in the Framework.

(iv.)   Settlement penalties are applicable to CSD participants, including CSDs when these have established a CSD link with a CSD applying CSDR SDR penalties.

---

[4] We understand that some flexibility until November 2020 may be provided by the policy makers, although this may only be confirmed in Q3 2019.

(v.) The parameters and penalty rates for the calculation of cash penalties for settlement fails have been adopted and officially published in March 2017 ("Cash Penalties Calculation Delegated Act").

(vi.) T2S CSDs and Eurosystem (via the "T2S CDR Task Force") jointly identified the necessary changes to the T2S platform and to facilitate T2S CSDs' compliance with CSDR.

As a result, the following documents were created (see Annex for details):

- T2S penalty mechanism document and subsequent specifications in the T2S Change Request 654;

- Penalty lists – Messages overview (ISO 20022 format, only; transposition into ISO 15022 messages is ongoing by SWIFT); and

- List of clarifications sent to ESMA (note that an additional list of items requiring clarifications has been submitted by ECSDA to ESMA).

Please note that a number of penalties-related elements mentioned in this Framework have been explicitly excluded from the T2S CSDR Task Force discussions and the documents resulting from it, such as:

i. Agreement on the list of financial instruments subject to penalties and sourcing of a "golden data feed" for the purposes of cash penalties calculation;
ii. Collection and redistribution of cash penalties (i.e. the actual payment of cash penalties); and
iii. Reporting and messaging from CSDs to their participants and between CSDs.

# 1 ECSDA CSDR PENALTIES FRAMEWORK KEY CONSIDERATIONS

1. The ECSDA Framework (market practice) is applicable to all CSDs subject to the EU CSDR or alike regulation[5]. The list of CSDs that subscribe to the Framework can be found in the Annex to the Framework[6]. In case a CSD cannot comply with the Framework in a specific aspect (due to e.g. legislative or operational boundaries), it will inform its participants accordingly.

2. The Framework aims at ensuring that all CSDs implement the provisions in a harmonised way, neutral of whether settlement takes place in or outside of T2S, and neutral to the systems that are used by CSDs to process settlement fails penalties.

3. The CSDR Penalties mechanism will be set up by all CSDs subject to CSDR. If a CSD already applies a penalties regime, this shall be adapted to or replaced by the CSDR SDR requirements. Beyond CSDR, CSDs may additionally introduce or use supplementary tools (e.g. if required by a regulator or deemed reasonable by the CSD for its local market) in order to ensure high settlement efficiency.

4. ESMA and T2S documents served as basis for creating this Framework. Large parts of the Framework are fully aligned and have been sourced from the discussions at the CSDR Task force as mentioned in the "T2S Penalty Mechanism" document (version October 2017) and the subsequent Change Request CR654[7]. The Framework also covers penalties related aspects that are not subject to the T2S CSDR Task Force documents (as they are not covered by the T2S scope as noted in the Framework Introduction).

5. This document may be subject to changes due to various working assumptions taken due to pending ESMA feedback or ongoing discussions within ECSDA or the market community.

6. The Framework is shared with other stakeholders (i.e. CSD participants, ECB, Central Counterparties, ESMA and other European Union and National authorities) with the aim of alignment and information sharing with relevant stakeholders.

7. According to CSDR and final ESMA RTS, the following principles must be applied by all EU CSDs:
   - A CSD shall provide for a cash penalty mechanism for participants that caused settlement fails.
   - Cash penalties are to be calculated on a daily basis for each business day that a matched (free, with or against payment) settlement instruction fails to settle on or after its Intended Settlement Date (ISD), including those instructions that are on hold or are failing due to a lack of cash.

---

[5] A CSD may decide to subscribe to the Framework also in cases when it is based in an EU third country jurisdiction and is subject to the legislation declared equivalent to the CSDR or even ahead of the recognition of non-EU legislation equivalent to the CSDR by the European Commission.

[6] Please see the list of CSDs using the Framework as the market practice in Annex IV.

[7] See ECB website for the latest version of the CR:
https://www.ecb.europa.eu/paym/target/t2s/governance/html/changerequests.en.html

- Penalties shall also apply to settlement of instructions matched in the securities settlement system *after* their ISD (e.g. due to instruction entry after ISD).
- Cash penalties are calculated *as from* the ISD until the actual settlement or cancellation date of the instruction, considering[8]:
  - Settlement Fail Penalty: once the instruction is matched, penalties apply earliest from the ISD or the matching date (when matching took place after ISD and no settlement occurred on the matching date) to the date of actual settlement or cancellation of the instruction, in addition to Late Matching Fail penalties, when applicable;
  - Late Matching Fail Penalty: penalties apply retroactively from the ISD until the actual matching date.
- As a general rule, penalty amounts shall be rounded up to maximum two decimals.
- For settlement fails involving multiple CSDs (cross-CSD settlements), SDR penalties, if applicable, shall be calculated only by one CSD, i.e. the CSD where settlement is actually taking place (based on the "actual place of settlement" concept). This also means that a CSD playing an Investor-CSD role, being a participant in another CSD (e.g. Issuer CSD) shall comply with the Terms & Conditions of the latter CSD.
- Daily reports shall be provided to the CSD participants in order to allow them to reconcile and calculate the recharge of the penalty to their underlying clients where applicable.
- The CSD must distribute the penalties only once they have collected them[9].
- The full amount collected as a penalty shall be redistributed to the participant that suffered from the fail at least on a monthly basis.
- Instructions with a CCP as counterparty:
  - CSD must calculate and report penalties for participants that are CCPs but not actually collect/ distribute any penalties;
  - CSDs must ensure that CCPs collect and redistribute fails penalties from/ to the relevant clearing members and provide a monthly report to the CSDs.
- The cash penalties shall not be configured as a revenue source for the CSD[10].

---

[8] Note: Both, a late matching fail penalty (LMFP) and a settlement fail penalty (SEFP), can apply on a single instruction; they may be charged to the delivering, receiving or both participants, depending on which of the two participants caused a) the late matching and b) the settlement fail. However, LMFP and SEFP cannot both apply for the same business day: either LMFP or SEFP can occur, depending on the matching timestamp (being before or after the CSD´s settlement cut-off time).

[9] The issue of partial receipts of payments is yet under discussion.

[10] However, CSDs have the possibility to charge for the cost of development and maintenance of their penalty system as a fee separate from the actual penalties amounts.

# 2 PENALTIES LIFECYCLE AND BUSINESS DAYS CALENDAR

This chapter covers penalties lifecycle events for both, intra-CSD and cross-CSD settlement fails scenarios:

A. **Daily events:**
   i. Daily Calculations
   ii. Daily Reporting
B. **Monthly events:**
   i. Monthly Appeal Period
   ii. Monthly Aggregated Amounts
   iii. Monthly Payment (Collection and Re-distribution)

*Note about the "appeal period": "appeals" refer to the exceptional correction or update of previously calculated and reported penalties upon CSD or participant request (e.g. due to the application of incorrect or updated reference data), and limited to the cases provided by ESMA CSDR Q&A.*

## 2.1 INTRA-CSD SETTLEMENT FAILS

Daily and monthly events are to be scheduled for the business days defined below.

### 2.1.1 Business Days

Applicable business days calendar:

- the CSD´s own settlement calendar[11];

- the payment system calendar of the relevant currency.

Business days are those days on which an instruction can settle in the own CSD <u>or</u>, in case of settlement versus payment, when the payment is executed outside the CSD system, the payment system applicable to the relevant currency ("opening days").

Based on the above, a penalty <u>shall not be applied when settlement is not possible</u>:

- 'free of payment' instructions: for the days when the CSD system is closed.

- 'against payment' instructions (when the payment is executed outside the CSD system): for the days when the CSD settlement system or the payment system of the relevant currency is closed.

Daily Calculations

A CSD shall calculate daily penalties for each instruction that:

   i. failed to settle on its intended settlement date (SEFP); or

---

[11] Note: the calendars of the CSDs and the payment systems should be retained for at least three months for penalties calculation purposes.

ii.     matched after its intended settlement date (LMFP).

For the computation of the Settlement Fail Penalties (SEFP), it is required to consider the (possibly different FOP and DVP) settlement cut-off times of the CSD.

For the computation of the Late Matching Fail Penalties (LMFP), it is required to consider the end of the business day as matching could still occur until then.

Daily penalties calculation for every single failed settlement instruction shall be completed by the CSD as soon as possible to make the daily reports available to its participants (including other directly linked CSDs) in a timely manner, i.e. optimally latest by midday (12:00 p.m. CET). No "intraday" penalties calculation or reporting applies.

These daily penalties reports might also contain a bilateral net of the penalties, per CSD, currency and counterparty (at the discretion of the CSD).

Daily penalties can only be calculated by CSDs when all relevant reference data is known.

For instance, the daily reference price of the security will likely only be available to CSDs during the following business day. As such, the penalties will be calculated for instructions that failed to settle on the previous business day (for cases when no daily price update is received by a CSD by this point in time, please refer to the assumption in chapter 5.2).

For every failing settlement instruction, the CSD will calculate, for each party[12], the net penalties (i.e. the single credit or debit net amount, not distinguishing between credit and debit net amounts, if this is used by the CSD) per CSD, currency and counterparty on a daily basis.

In case of penalties removal, re-integration and/ or re-calculation, updated net penalties per counterparty and currency will be provided.

Under exceptional circumstances (see ESMA CSDR Q&A "Settlement Discipline Questions 4 – Cash penalties: scope"), daily penalties, previously calculated by the CSD for the current calendar month, could be amended (i.e. re-calculated due to changes in applicable reference data) or removed (i.e. cancelled) on any business day until the appeal period has ended (see chapter 2.2.1.4 for details).

Daily penalties previously removed by the CSD, for the current calendar month, could be re-included on any business day until the appeal period has ended. If the applicable reference data has changed, the penalty will be re-calculated.)

The penalties calculation rules as well as the reference data used in the calculations are described in chapter 7.

---

[12] Due to local or settlement platform specifics, the definition of 'party' remains at the discretion of each CSD that will decide at which level it  applies the 'party' concept (level of the entity, LEI, BIC, participant securities account, or other; note: for T2S, only BIC is allowed).

### 2.1.2 Daily Reporting

CSDs will send a daily penalty report to their participants when there are new, amended, removed or re-included penalties during the day.

The penalty calculation period shall be one calendar month. For each business day, CSDs may generate:

- either a single report; or
- two separate reports, one for the new penalties and one for the amended, removed or re-included ones, if applicable.

## First MONTH (computation and reporting of penalties)



Daily reporting of penalties computed for 1st business day of the month

Daily reporting of penalties computed for last business day of First month
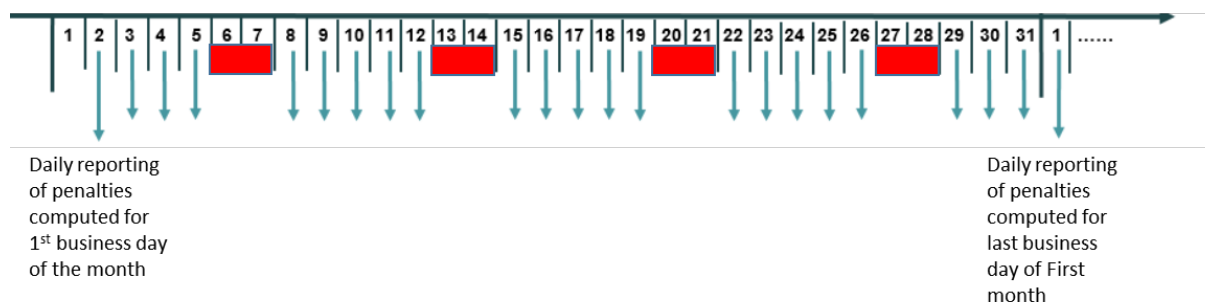
The report of modified penalties (if applicable) may include various business days, however, the new bilateral net amount per counterparty and currency has to be provided by business day.

CSDs shall report penalties for each "party" and aggregated per counterparty (a participant in this same CSD).

OPEN ITEM ECSDA: according to current discussions within ESCDA, a "party" may be defined by a CSD either on BIC (approach as applied by T2S) or CSD participant account number or LEI level. However, the topic is still under review by ECSDA as e.g. the CSD-role under national law and domestic market models may have to be considered as well in this respect. Hence, the usage of harmonised definitions across all CSDs is unlikely to be achievable.

In the case of no penalty is to be applied (no failed transaction resulted in new penalties, amendments, removals or re-inclusions) for one reporting day, for a party, a report stating "no activity" may be sent[13]. CSDs shall deliver the daily reports to their participants after the closing of the settlement day (on which (new or previous) penalties were calculated, amended, removed or re-included) and latest until midday (12:00 p.m. CET) on the following business day. Penalties for fails on a Friday might be calculated and reported either on Saturday, or Sunday, or Monday morning, depending on the CSD's own operational day (but in all cases the business date shall be the one of Monday).

---

[13] CSDs may offer 'no activity' reports upon subscription so its participants will be able to choose to receive 'no activity' reports or not.

Messaging and report aspects are covered in chapter 11 of this document.

### 2.1.3   Monthly Events

All CSDs shall follow the same monthly timetable to ensure that the appeal period and penalty finalisation occur on the same date.

ECSDA may maintain a 'Penalties calendar' indicating the closing dates throughout the year for settlement and payment systems that shall be considered by all CSDs subject to SDR and used in regard to the penalties payment process business days.

The below timeline for the monthly reporting, assessment and payment process applies:



## Following MONTH (provision of aggregated amounts and payment)

**Daily reporting of penalties computed for last business day of previous month (i.e. First month)**

**End of appeal period: 10th BD** = Last day to ask for corrections on penalties from previous month.

**12th BD COB** = Last day to input amendments

**14th BD = Provision of Monthly aggregated amounts** for penalties of previous month (i.e. of First month) including cross-CSD penalties

**15th BD =**
- Calculation of the **net amount to be received OR paid including cross-CSD penalties**
- Reporting of the **Cash pre-advice**

**17th BD = Payment**
1- Collection
2- Redistribution

Messaging and report aspects are covered in chapter 11 of this document.

### 2.1.4   Monthly Appeal Period

CSDs shall apply a dedicated appeal period for CSD participants to assess single settlement fails penalty calculations, <u>on an exceptional basis,</u> within and post the end of a calendar month.

Reasons for appeals may be the situations listed in the ESMA CSDR Q&As "Settlement Discipline Questions 4 – Cash penalties: scope":

- ISIN suspension from trading[14] or settlement (e.g. due to "undue creation or deletion of securities" reconciliation issues);
- Settlement instructions involving cash settlement outside the securities settlement system operated by the CSD if, on the respective day, the relevant payment system is closed for settlement;
- Technical impossibilities at the CSD level that prevent settlement, such as: a failure of the infrastructure components, a cyber-attack, network problems.

The appeal period ends at close of business on the 10th business day of the following month for CSD participants.

Appeals can be lodged by CSD participants at any time during the calendar month, as from the moment of computation and reporting of the penalty, and until (and including) the 10th business day of the following month.

Any amendment requested after the appeal period ended cannot be taken into account by the CSD.

Each time that an appeal is accepted by a CSD, and a change is applied to a penalty, it will be reported on the following business day. Updates made by the CSD on the 11th business day of the following month will be reported on the 12th business day of the following month (the same way as it is done for any other business day).

By close of business on the 12th business day of the following month, any adjustment resulting from appeals shall be completed by the CSD, to be reported on the 13th business day of the following month by midday (12:00 p.m. CET) at the latest.

In order to apply for an appeal, sufficient information needs to be provided by the CSD participant to the CSD, covering at least:

- the reference of the penalty as well as the failed transaction,
- the reason for the appeal; and
- the expected penalty amount and calculation details to be applied.

Appeals represent an exception handling by CSDs; unless agreed otherwise in ECSDA, each CSD will design its own processes considering e.g. its GTCs, communication requirements to submit an appeal and provide the outcome of the appeal assessment to their participants.

### 2.1.5    Monthly aggregated amounts

On the 14th business day of the following month, the CSD will report the monthly aggregated amounts for the penalties of the previous month (i.e. the aggregated amounts of the penalties computed for the business days of the previous month).

---

[14] While this is stated in the ESMA Q&As, ESMA advised ECSDA this is not meant to be mandatory but a non-exhaustive example for cases when CSD may not need to apply penalties. In this specific case, CSDs are usually not aware of the suspension taking place at trading level.

For each party, per currency and counterparty, the CSD will sum up all the cash penalties that this party can be expecting to be credited and debited by this counterparty.

If the net-result is a credit, the party can expect a cash payment from this counterparty. If the result is a debit, the party will have to pay this counterparty.

Thus, the monthly reporting shall include, per currency and per party, all the net amounts against each of its counterparties for the penalties computed for the business days of the previous month.

Note: the monthly reports will not include the details of each gross penalty (that is only available in the daily reports).

For additional information on the monthly aggregated amounts, please refer to chapter 7.4 "Monthly cash penalties aggregation".

### 2.1.6 Monthly payment (collection & re-distribution)

On the 17th business day of the following month, the CSD (and its participants) shall perform the payment process, i.e. the CSD shall collect and re-distribute the penalties amounts to/ from its participants.

Note: for each party, the net amount (to be paid or to be received) shall be reported by the CSD latest on the 15th business day thereby providing time to perform FX transactions (if required) before the payment date (17th business day). Fails involving CCPs are excluded from the monthly payment process (but part of the daily and monthly reports).

As described in chapter 10, depending on their set-up (having/ not having a banking license) and national specificities, CSDs will use different models for the actual penalties payments processing.

The following possible payment models were identified:

1. CSD triggers direct debits and/ or cash transfers;
2. CSD generates PFOD instructions;
3. Usage of a payment bank.

CSDs may define appropriate measures (to be described in the relevant contractual documents with the CSD participants) to ensure penalty amounts due are available to the CSD and CSD participants comply with their payment obligations to the CSD on time on the 17th business day to avoid delays and processing issues due to a lacking or incomplete penalties collection.

For additional information on the monthly payment process, please refer to chapter 10 .


## 2.2 CROSS-CSD SETTLEMENT FAILS (FOR CSD DIRECT LINKS TO OTHER CSDS)

Daily and monthly events apply for the business days defined below.

### 2.2.1 Business Days

Applicable business days calendar:

- the CSD´s own settlement calendar;

- the penalties Calculating-CSD´s settlement calendar[15];

- the payment system calendar of the relevant currency.

Business days are those days on which an instruction can settle in the Calculating CSD´s settlement system and (in case of settlement versus payment, when the payment is executed outside the CSD system) the payment system applicable to the relevant currency ("opening days").

In order to allow CSDs to be able to assess the relevant European CSD´s opening days for securities and cash processing, the relevant information shall be provided to ECSDA by the respective CSDs and be made available centrally by ECSDA (to CSDs, CSD participants and general public).

ECSDA may maintain a 'Penalties calendar' indicating the closing dates throughout the year for settlement and payment systems that shall be considered by all CSDs subject to SDR in regard to the penalties payment process business days.

Based on the above, a penalty shall not be applied when settlement is not possible, i.e.:

- for 'free of payment' instructions: for the days where the Calculating CSD was closed, thus when a settlement instruction cannot settle in the CSD´s system;

- for 'against payment' instructions (when the payment is executed outside the CSD system): for the days where the Calculating CSD´s settlement system or the payment system of the currency was closed, thus when a settlement instruction cannot settle in the CSD´s system and/ or in the payment system of the currency.

Daily Calculations

The same process than the one mentioned in chapter 0 shall apply when the CSD is acting as an issuer CSD (for an investor CSD).

In line with the "actual place of settlement" concept, if the CSD is acting as an investor CSD, it shall wait for the daily amounts to be provided by the Calculating CSD where settlement is actually taking place and report them afterwards to its own participants.

To avoid procedural complexity and reconciliation issues, the investor CSD shall not make own penalty calculations but rely on the Calculating CSD[16].

---

[15] Note: The calendars of the CSDs and the payment systems should be retained for at least three months for penalties calculation purposes.

[16] If all involved CSDs are subject to CSDR, only the CSD where settlement is actually taking place shall calculate the penalties; all CSDs involved will have to report and collect/ re-distribute. Note for T2S external settlement, T2S will (until further notice) calculate in any case. It will be up to T2S CSD to remove these penalties and replace them by the ones reported by the Calculating CSD. Please refer to chapter 9 "Cross-CSD settlement fails" and Annex for a description of all settlement scenarios.

The daily calculation performed by the Calculating CSD considers the Investor-CSD as a standard participant (in the other CSD´s books). It means that the Calculating-CSD cannot provide the daily penalties at the level of the Investor CSD´s participants.

The Calculating CSD shall report the daily penalties to the investor CSD, as soon as possible and optimally latest by midday (12:00 p.m. CET), in order for the investor CSD to report these cross-CSD penalties in a timely manner to its own participants[17].

### 2.2.2 Daily Reporting

The same process than the one mentioned in chapter 2.1.2 shall apply when the CSD is acting as penalties calculating Issuer CSD (for an Investor-CSD).

CSDs shall send a daily penalty report to their CSD participants when there are new, amended, removed or re-included penalties.

The daily reporting can segregate the penalties resulting from the intra-CSD activity, and the ones resulting from the cross-CSD activity. In such a case, the CSD participant might receive up to four reports, for the same business day:

- a report including all new intra-CSD penalties;
- unless included in the "new penalties" report, a report including the penalties intra-CSD which were amended, removed or re-included;
- a report including all new cross-CSD penalties;
- unless included in the "new penalties" report, a report including the penalties cross-CSD which were amended, removed or re-included.

Calculating CSDs (and, upon receipt from the Calculating CSD, Investor-CSDs) shall deliver the daily reports to their participants until midday (12:00 p.m. CET) on the following business day at the latest. The receiving CSD will in turn report these penalties to its participants. Thus, such penalties may be reported <u>after</u> midday (12:00 p.m. CET) on this same business day (depending on the time of receipt from the Calculating-CSD).

The penalty information shall be passed on to the 'failing party' of the failing settlement instruction, as it appears in the the CSD records.

In case of a CSD link, the failing party may be a participant or an underlying client of a participant of the relevant linked CSD. In case of indirect and operated direct[18] links, the information flow is longer compared to a direct link. It could go from the CSD reporting the penalties to the intermediary acting on behalf of the CSD to the customer of the intermediary (i.e. the CSD), and then to the underlying CSD participant. How this information flow is technically ensured is subject for specification by the involved CSDs.

---

[17] CSD participants may receive the reports on intra-CSD penalties and the reports on cross-CSD penalties in different batches during the day.
[18] Operated means the CSD has a direct link/ account with the other CSD that is operated by an agent.

### 2.2.3    Monthly Events

The monthly events, in a cross-CSD scenario, are identical to the ones in an intra-CSD scenario for the 'First month'.

A difference applies related to the end of the appeal period (as highlighted in red).

## Following MONTH (provision of aggregated amounts and payment)



| Daily reporting of penalties computed for last business day of previous month (i.e. First month) | **End of appeal period:** 11<sup>th</sup> BD = Last day to ask for corrections on penalties from previous month. | **12<sup>th</sup> BD COB** = Last day to input amendments | **14<sup>th</sup> BD = Provision of Monthly aggregated amounts** for penalties of previous month (i.e. of First month) including cross-CSD penalties | **15<sup>th</sup> BD =** - Calculation of the **net amount to be received OR paid including cross-CSD penalties** - Reporting of the **Cash pre-advice** | **17<sup>th</sup> BD = Payment** | 1- Collection 2- Redistribution |

### 2.2.4    Monthly Appeal Period

In a cross-CSD context, the appeal period ends at close of business on the 11<sup>th</sup> business day of the following month. It allows CSDs to pass on to other CSDs the appeals requested by CSD participants on the 10<sup>th</sup> business day. At close of business on the 11<sup>th</sup> business day of the following month, CSDs shall no longer request appeals to other CSDs.

An appeal requested latest until the 10<sup>th</sup> business day by a CSD participant (in line with chapter 2.1.5) and accepted by a CSD, must be sent to the other CSD on the 11<sup>th</sup> business day, and thus will be reported to the CSD participant on the 12<sup>th</sup> business day (depending on the settlement chain).

By close of business on the 12<sup>th</sup> business day of the following month, any adjustment resulting from appeals shall be completed by the CSD, to be reported on the 13<sup>th</sup> business day of the following month by 12:00h a.m. CET at the latest.

### 2.2.5    Monthly aggregated amounts

The process will be identical to the one described in intra-CSD. The monthly aggregated amounts will include the cross-CSD penalties sorted by CSD.

In a cross-CSD scenario, the monthly aggregated amounts will be calculated per CSD link, meaning that the bilateral net amounts will be calculated for each CSD, per currency and counterparty.

For additional information on the monthly aggregated amounts, please refer to chapter 7.4.

### 2.2.6    Monthly payment (collection & re-distribution)

In a cross-CSD scenario, the process will slightly differ compared to 2.1.6, as CSDs are not themselves the ones responsible for supplying the funds to proceed with the penalties payment.

On the 17th business day of the month, all involved CSDs shall have collected the amounts due by their participants (including those that are CSDs themselves), in order to be able to start the payment process across CSDs (note: the 'direct debit' process is usually not available in a cross-CSD direct-link scenario).

One full net per CSD link will be provided on the 15th business day. For each of its participants being a CSD, the Calculating-CSD will provide a single net, being the amount to be received minus the amount to be paid. If the result is a credit, then the Calculating-CSD will expect payment from the other CSD(s). If the result is a debit, then the Calculating-CSD will have to pay the other CSD(s).

Note: it is not possible to sum some amounts that pertain to various CSD links. Hence, the Calculating-CSDs shall calculate a single amount per every CSD-link and currency.

WORKING ASSUMPTION (ESMA to confirm): Once the cash due is received from the CSD participants (that are not CSDs), the CSD will pay the other CSDs. In parallel, this CSD will receive the cash it expects from the other CSDs.

Each CSD will have to pay (for each currency, if applicable) the exact amount as reported by the other CSD.

CSDs may define appropriate measures (to be described in the relevant contractual documents with the CSD participants) to ensure penalty amounts due are available to the CSD and CSD participants comply with their payment obligations (in each currency reported) to the CSD on time on the 17th business day to avoid delays and processing issues due to a lacking or incomplete penalties collection.

# 3   PENALTIES SCOPE

## 3.1   INSTRUCTIONS SUBJECT TO CASH PENALTIES – GENERAL SCOPE

Settlement fails penalties shall be calculated for all settlement instructions, free of or against / with payment that are:

- "transfer orders[19]" according to the second indent of point (i) of Article 2 of Directive 98/26/EC [Settlement Finality Directive], and
- matched (prior, on or after their Intended Settlement Date (ISD)), and
- failing to settle on and after their ISD,

WORKING ASSUMPTION (ESMA to confirm): The only exemptions are:

- Redemptions (ISO Transaction Code equals REDM);
- Corporate actions on stock (ISO Transaction Code equals CORP);
- Technical instructions, e.g. T2S automatic realignments;
- T2S Settlement restrictions[20]

Note:

- (T2S) Auto-collateralisation operations, while automatically generated, are considered in scope;
- OPEN ITEM (ESMA to clarify): Primary issuance settlements are in scope (except the process of initial creation of securities which cannot be regarded as a "transfer order" from a legal standpoint[21]);
- OPEN ITEM (ESMA to clarify): treatment of Investment Funds order routing instructions (CSD model vs. TA model/ transfer order vs. settlement instructions model).

For CCP-related aspects, please refer to chapter 12.3.

## 3.2   INSTRUCTIONS SUBJECT TO CASH PENALTIES - CROSS-CSD SETTLEMENT SCOPE

In context of settlement transactions beyond the CSD´s own system, various scenarios were elaborated by T2S CSDR TF and ECSDA, and yet to be officially endorsed by ESMA. These must be considered by CSDs to define if a failing instruction is actually subject to penalties; please refer to Chapter 9 for details.

---

[19] Definition: "Any instruction by a participant to place at the disposal of a recipient an amount of money by means of a book entry on the accounts of a credit institution, a central bank, a central counterparty or a settlement agent, or any instruction which results in the assumption or discharge of a payment obligation as defined by the rules of the system, or an instruction by a participant to transfer the title to, or interest in, a security or securities by means of a book entry on a register, or otherwise."

[20] A T2S Settlement restriction is an Intra-position movement. It is used to manage restriction on a securities position which can be: a securities blocking; a securities reservation; or a securities earmarking.

[21] T2S CSDR TF wording; note re. Investment funds issuance (creation/ redemption), based on ECB feedback: unlike for corporate actions where the Issuers are paying CSD participants, there is generally no obligation on the side of participants, for Issuance and Fund Investment the counterparties are CSD participants who are buyers, so these shall be considered as normal transactions, subject to penalties.

In summary, an "actual place of settlement" concept applies:

- when the actual settlement is taking place in a CSD subject to CSDR, penalties shall be calculated and applied by this CSD ("Calculating CSD"); the (Investor-)CSD being a participant of the other CSD is obliged to report the penalties further to its own participants and also perform the cash collection and redistribution process;
- when the actual settlement is taking place in a third-country CSD (not subject to CSDR), no (CSDR) penalties shall apply.

Notes regarding T2S:

- T2S will always calculate and report the penalties, even if it is not the place of settlement or involving the Issuer CSD.

- when settlement takes place between two Investor-CSDs, the subsequent realignment transactions on Issuer-CSD level shall not be subject to settlement fails penalties, independent if the Issuer-CSD is inside or outside T2S. See also chapter 3.1.

## 3.3  INSTRUMENTS SUBJECT TO PENALTIES

Settlement fails penalties must be calculated in case a matched settlement instruction in scope of SDR is failing to settle and the instrument to be transferred is:

- a CSD-eligible MiFID/R financial instrument:
    - admitted to trading or traded on an EU trading venue (see ESMA FIRDS database[22]); or
    - cleared (or eligible for clearing) by an EU CCP.
- excluding shares when their principal trading venue is located in a Third Country[23].

Note: the relevant MiFID/R financial instruments types are:

- transferable securities [i.e. equity- and bond- (like) instruments (including ETFs) and giving a right to buy or sell any of those],

- money-market instruments,

- UCITS and

- emission allowances.

I.e. to derive the concrete list of ISINs subject to SDR, a CSD shall

---

[22] https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_firds

Note: while "complete" and "delta" lists are provided; CSDs are recommended to refer to the "complete" file for their daily updates to ensure full ISIN coverage. As the FIRDS database also contains instruments that are not CSD-eligible (like derivatives), CSDs should limit the query to instruments being eligible in their CSD settlement system.

[23] CSDR Art. 7.13 states: "This [CSDR] Article [7] shall not apply where **the principal venue for the trading of shares** is located in a third country. The location of the principal venue for the trading of shares shall be determined in accordance with Article 16 of Regulation (EU) No 236/2012." See "Short Selling Regulation (SSR)" exempted instrument list: https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_mifid_shsexs

a) use the ESMA FIRDS database for MIFID/R instruments;
b) identify the ISINs eligible for settlement in the CSD; and
c) eliminate those shares that are exempted from the Short Selling Regulation.

As the FIRDS database is updated daily at 09.00h a.m., in order to avoid discrepancies between CSDs and to be in line with T2S processing timelines, CSDs shall always consider the FIRDS database as available at the end-of-fail day (example: fail date 15.04.19; penalty calculation date/ time 16.04.19 10:30h a.m. → FIRDS db published as of 15.04.19 **end of day** shall be used).

Please also refer to chapter 5 for the reference data required to calculate penalties.

# 4 IDENTIFICATION OF THE PARTY TO BE PENALISED

## 4.1 LATE MATCHING FAIL PENALTY (LMFP)

Any settlement instruction being in scope of the penalties calculation that is matched **after** the relevant CSD settlement cut-off time of its ISD will be subject to computation of Late Matching Fail Penalties (LMFP) for the business day when it is matched <u>and</u> (retroactively) for each past business day that it failed to settle.

The penalty is charged to the participant who was last to enter or modify the relevant settlement instruction (e.g. 'accepted timestamp' is later than the one of the counterparty´s instruction) for the periods between the ISD and the day of matching of the instruction.

Note that even in cases when both parties send their instructions "late" after the ISD, only one of the two counterparts of a transaction shall be imposed with a LMFP.

I.e. the party with e.g. the earlier 'accepted timestamp' of its settlement instruction will not be considered as a failing party and hence no penalty will be imposed to this party in relation to the late matching.

Please also refer to chapter 7 (special handling in case of only partially successful buy-ins).

### 4.1.1 LMFP special case: Already matched instructions

<mark>ASSUMPTION (ESMA to confirm):</mark> If a CSD is offering the possibility to send settlement instructions as already matched (i.e. both instructions are sent at the same time as matched, often used for CCP instructions), these settlement instructions will be subject to computation of LMFPs in case they are sent late.

It is not always possible for the CSD to determine the failing party by comparing the accepted timestamps (as both legs have the same timestamp).

In some cases, the penalty will be applied to the instructing party of the two settlement instructions (i.e. the party who sent the instructions to the CSD). Therefore, it will be up to the instructing party (e.g. CCP) to inform the CSD to whom to allocate the penalty (i.e. the delivering or the receiving participant) and enable the CSD to adjust the penalty assignment accordingly[24].

In other cases, the penalty might not be applicable to the instructing party of the two settlement instructions, as this instructing party does not have an account in the CSD books (e.g. electronic trading platforms). In such a case, the delivering party might be the one to be penalised by default. It will be up to the delivering party, in agreement with the instructing party, to request the CSD to perform a re-allocation of the penalty to the receiving party if it was the real defaulting party.

---

[24] Such a case will likely be very rare, as CCPs are normally sending their settlement instructions at the opening of the operational day (D-1 of the business day) and prior to ISD.

## 4.2 SETTLEMENT FAIL PENALTY (SEFP)

Any settlement instruction, being in scope of the penalties calculation, that

- i) is matched **before** the relevant cut-off of a given business day; and
- ii) has reached its ISD; and
- iii) **fails to settle** on that ISD or on the day it is matched (late, after ISD) and after

shall be subject to computation of Settlement Fail Penalties (SEFP) for each business day the instruction is failing to settle.

A settlement instruction that "fails to settle on that ISD" must be understood as a settlement instruction that is not cancelled and remaining to be settled, fully or partially, by the time of the end of processing of the relevant CSD settlement cut-off time.

The end of processing of the relevant cut-off of each settlement instruction is the key point in time to take a "snapshot" of the status and fail reason of a settlement instruction and determine its eligibility for penalty application. A penalty shall be imposed to a CSD participant if its settlement instruction fulfils, at the time of the end of processing of the relevant cut-off, any of the below conditions:

- the instruction is **on hold** (any type of hold); or
- the instruction **failed the settlement eligibility or provision check**, i.e. the fail reason associated to this instruction is **"lack of securities" or "lack of cash"**. Note: when "lack of securities is identified" no additional fail check for a "lack of cash" shall be made by the CSD.

Note that it is possible that the two counterparts of a transaction are imposed with a SEFP, for example, when both legs of a matched instruction are on hold until the CSD settlement processing cut-off time. In such scenario, both parties will be imposed with a SEFP (i.e. the delivering party will be charged with "lack of securities" penalties, the receiving party with "lack of cash" penalties).

# 5 REFERENCE/ STATIC DATA REQUIRED FOR PENALTY CALCULATIONS

In order to calculate the daily settlement fails penalties, the information described in this chapter needs to be available to or sourced by CSDs.

When reference data (e.g. CFI code, security reference price) required to calculate penalties is missing by the calculation date, penalty amounts shall be set to "zero" until the data becomes available.

The latest point in time for consideration of new (or updated) reference data by the CSD shall be the 11th business day of the following month. That means that if new or updated data for calculating penalties is available to the CSD only after the 11th business day, no retroactive penalties calculations or adaptations should be made by CSDs.

Please refer to chapter 8 related to updated reference data leading to changes of previously calculated penalties.

## 5.1 LIST OF INSTRUMENTS SUBJECT TO PENALTIES
For the identification of instruments in scope, please refer to chapter 3.3.

## 5.2 DAILY REFERENCE PRICE

CSDs need to source (or derive) and apply a reference price for each day when the settlement instructions fails to settle. It shall be in line with CSDR price determination rules[25], for those securities eligible for settlement in the CSD and whenever the instrument is in the scope of the CSDR penalty regime:

- instrument is in scope of MiFID/R (see ESMA FIRDS database):

  - shares and similar: closing price of the "most relevant market" (MRM) in terms of liquidity (MRM information is available in the FIRDS database);

  - other instruments: closing price of the trading venue "with the highest turnover" (OPEN ITEM (ESMA TO ADVISE): HOW CAN "HIGHEST TURNOVER" INFORMATION ACTUALLY BE DERIVED BY DATA VENDORS OR CSDs?);

  - WORKING ASSUMPTION (ESMA to confirm): for instruments for which no updated daily MiFID/R price is available, use the latest MiFID/R price or - when no MiFID/R price is available at all - a price as determined by the CSD.

- Considering the above, for MIFID/R instruments, CSDs must source (usually via their data vendors) the applicable prices from the MIFID/R Trading Venue relevant for a single
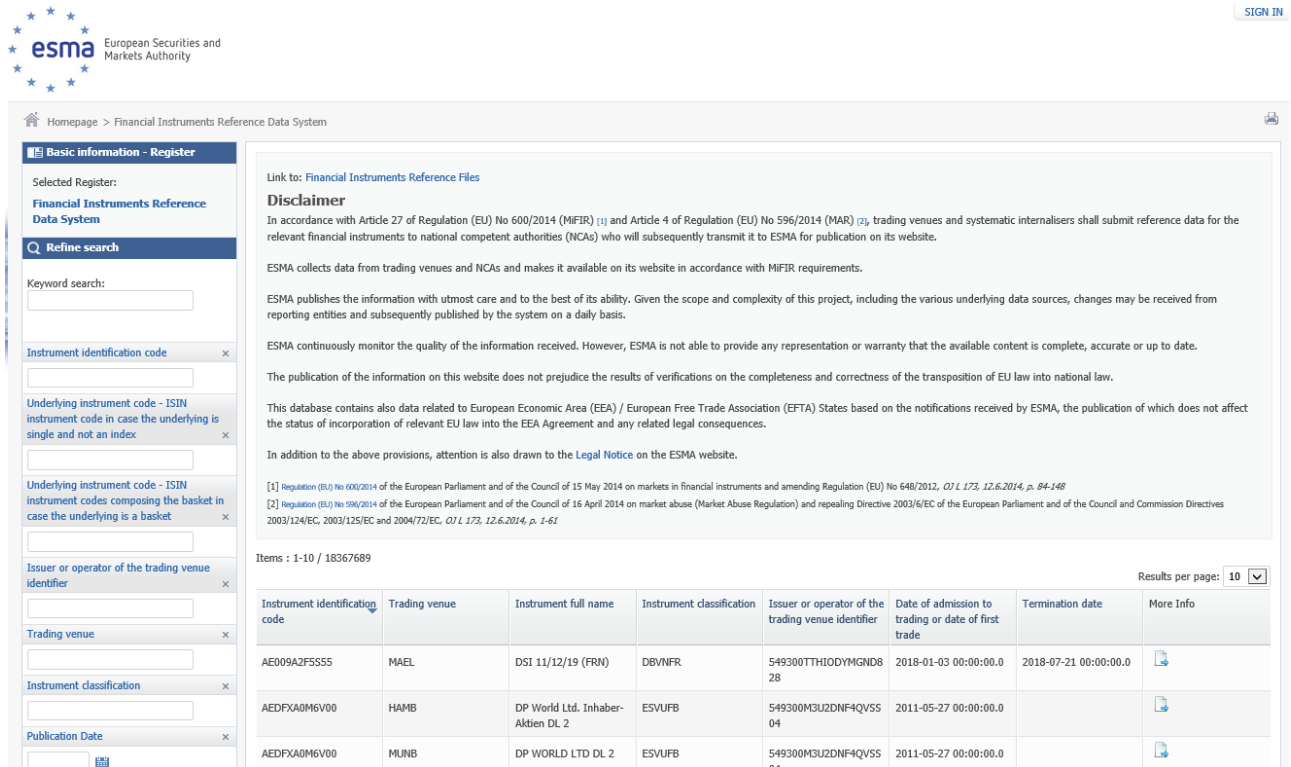
---

[25] See Article 7 of the Delegated Regulation: http://eur-lex.europa.eu/eli/reg_del/2017/389/oj

instrument, using the ESMA FIRDS database (note: ESMA does **not** publish the trading prices):

- – https://www.esma.europa.eu/databases-library/registers-and-data

- – use file "Financial Instruments Reference Database (FIRDS)" to open:

https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_firds



Due to the huge size of the database, the data must be extracted electronically and checked for relevant updates on a daily basis.

By following this information sourcing process, the reference prices applied by CSDs are expected to be identical for a single instrument that can be settled in multiple CSDs.

- Instrument is out of MiFID/R scope:

- – market price determined by the CSD, according to its price determination method as approved by the CSD´s National Competent Authority[26];

- – WORKING ASSUMPTION (ESMA to confirm): where no market value is available, CSDs will use:

---

[26] In such case, the reference prices applied by CSDs may deviate for a single (EU or non-EU) instrument that can be settled in multiple CSDs. However, the impact would be limited to intra-CSD settlement fails (as for cross-CSD settlement fails, the "actual place of settlement" concept applies, see Chapter 9).

- for debt instruments: nominal value (in the ISIN denomination currency);
- for non-debt instruments: default price (e.g. issue price).

The daily reference price used for calculating the fails penalties is the price of each business day when the settlement instruction is subject to penalty calculation (i.e. using maximum three months of historical prices when relevant, e.g. for late matching fails), independently from when the calculation is actually performed.

That means that the reference price for the penalty calculation of each fail day shall be the one of the relevant fail date.

For example: a FOP instruction with Intended Settlement Date 05.10.18 only matches (but does not settle) on 07.10.18 – reference prices for 05.10., 06.10. (for LMFP calculation) and 07.10.18 (for SEFP calculation) are to be applied, assuming these are business days and the CSD system was open for settlement).

Therefore, CSDs are required to source and store market price data for all instruments in scope of the penalty regime on a daily basis[27]. In the absence of a single European price feed or source for all CSDs, this has to be managed individually by CSDs via their data vendors, unless CSDs can source price data themselves.

Note that reference price data shall not be reported or otherwise made available to parties other than the responsible CSD or its penalties mechanism provider (i.e. the penalty messages as described in chapter 11 shall contain "NONREF" or remain blank in the respective price fields).

The application of identical reference prices for the same ISIN by CSDs in a cross-CSD settlement context is ensured by the process design as CSDs shall always use the penalties calculation as provided to them from the Calculating CSD where settlement is actually taking place ("actual place of settlement" concept; see detailed scenarios in Chapter 9), i.e. the penalties as calculated and reported by this CSD to its participants (that may as well be CSDs) shall always be applied as such by the CSDs involved in the settlement chain. Price data must be available before daily penalties applicable for the single fail date can be calculated. CSDs shall, therefore, send the penalties data and reports to their customers including other CSDs latest by midday (12:00 p.m. CET) (see Chapter 2 for details).

The amount imposed by the penalty shall be calculated:

- for against payment settlement fails:

    1. in the currency of the cash leg.

- for free of payment settlement fails:

---

[27] For instruments with specific features like pool factors, CSDs shall apply the price as sourced from the Trading Venue or determined by the CSD, without any special modifications for penalties calculation purposes.

1. either in the currency of the underlying security if the instrument is quoted in nominal or per cent (usually Fixed Income instruments); or

2. in the currency of the daily reference price if the underlying security is quoted in units (usually shares);

3. or a default currency as defined by and eligible for settlement in the Calculating CSD

This may lead to a FX conversion need (see Chapter 6 for details).

## 5.3 INSTRUMENT TYPE

1. <mark>WORKING ASSUMPTION (ESMA to officially confirm)</mark>: Instrument type classification will be derived from a CFI code mapping table, to be maintained by ESMA.

The "Financial Instrument Type" is a classification of securities according to which CSDs shall report settlement fails to regulators, as laid out in the CSDR SDR RTS Annex 1, table 1[28].

This classification is also relevant, together with the Liquidity and SME Growth Market classifications for the identification of the applicable penalty rate for any given failed settlement instruction.

Therefore, CSDs shall, for each security, derive the Financial Instrument Type classification from the CFI Code of the same security, according to the following mapping table (currently under review by ESMA; source: T2S CR654 dd. 04.10.2018):

| CFI Code Structure | Type of Financial Instrument |
|---|---|
| **Position 1 of the code is "E"** | SHRS |
| **Position 1 of the code is "D" and position 4 is "T" or "C", or position 2 is "N"** | SOVR |
| **Position 1 of the code is "D", position 2 is neither "Y" or "N" and Position 4 is neither "T" nor "C"** | DEBT |
| **Position 1 of the code is "R"** | SECU |
| **Position 1 of the code is "C" and position 2 is "E"** | ETFS |
| **Position 1 of the code is "C" and position 2 is not "E"** | UCIT |
| **Position 1 of the code is "D", position 2 is "Y" and position 4 is neither "T" nor "C"** | MMKT |
| **Position 1 is "T", position 2 is "T" and position 3 is "N"** | EMAL |
| **Residual category** | OTHR |

---

[28] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2018.230.01.0001.01.ENG&toc=OJ:L:2018:230:TOC
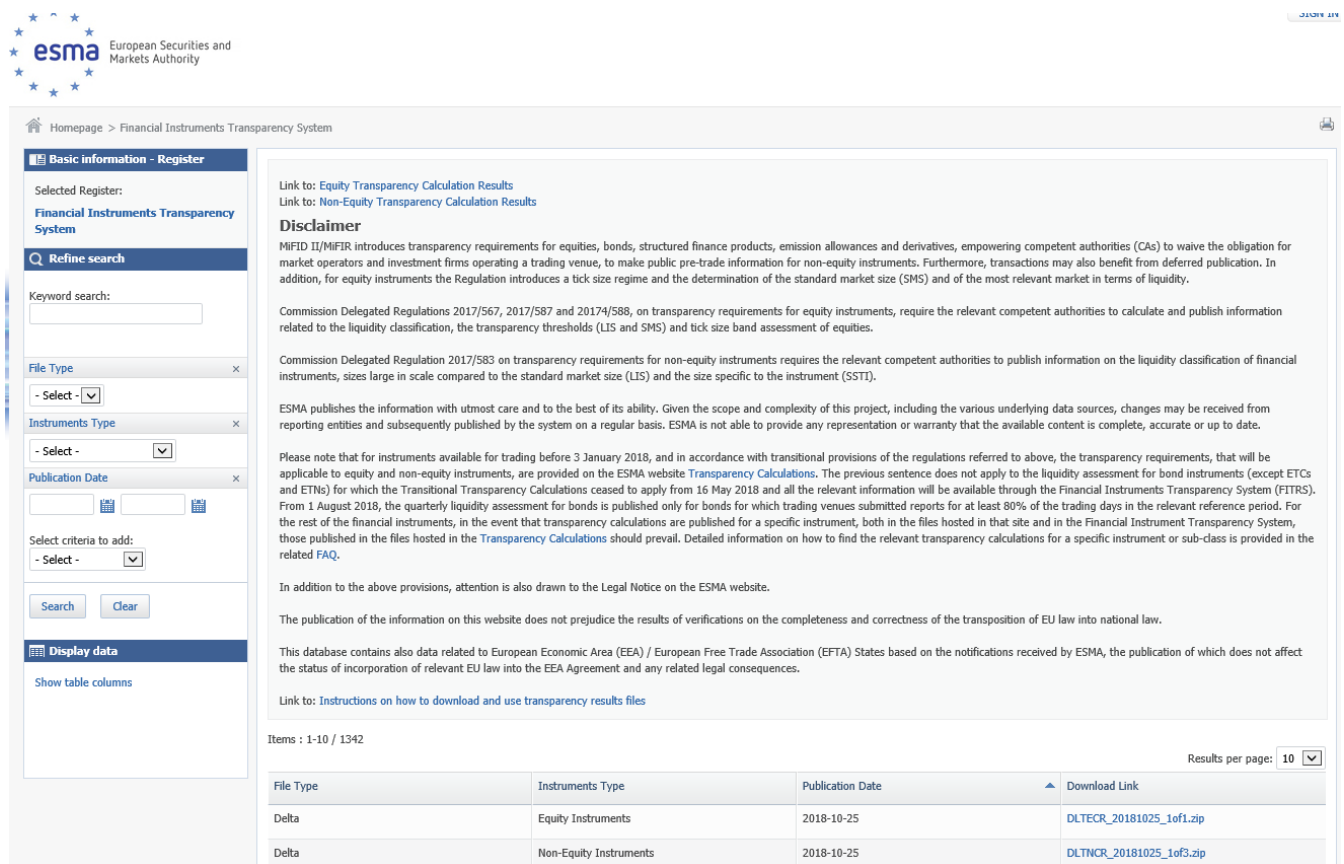
## 5.4 INSTRUMENT LIQUIDITY/ILLIQUIDITY CLASSIFICATION

The liquidity indicator is a binary classification of securities that, for the purpose of penalties calculation, only applies to shares, i.e. when the Financial Instrument Type of the security is "SHRS" and specifies if the security is "Liquid" or "Illiquid"[29].

This classification of securities is an attribute of the securities subject to penalties and must be derived by the CSDs from the ESMA database (WORKING ASSUMPTION, ESMA to confirm):

https://www.esma.europa.eu/databases-library/registers-and-data

Use file "Financial Instruments Transparency System (FITRS)" to open and filter on "Instrument Type" equals "Equity Instruments".



---

[29] The ESMA FITRS database also covers debt instruments liquidity indicators; however, the CSDR penalty rates to be applied (see chapter 5.6) do no refer to liquidity aspects for debt instruments. Note: while "complete" and "delta "lists are provided; CSDs are recommended to refer to the "complete" file for their daily updates to ensure full ISIN coverage.

## 5.5 INSTRUMENT TRADING SEGMENT "SME GROWTH MARKET" - PLACE OF TRADING INFORMATION

The SME Growth Market indicator is a binary classification of securities that applies for any type of securities and that specifies whether the security is listed in a SME Growth Market.

For the sake of identifying the applicable penalty rate, CSDs need to identify whether the instrument to be settled was actually traded on an EU SME Growth Market by verifying both, the receiving and delivering instruction, of the settlement transaction.

Only when both instructions show the same "Place of trading" four-digit MIC (Market Identifier Code), the reduced penalty rate applicable to SME instruments shall be applied.

The list of SME Growth Market Trading Venues can be found on the ESMA website:

https://www.esma.europa.eu/databases-library/registers-and-data
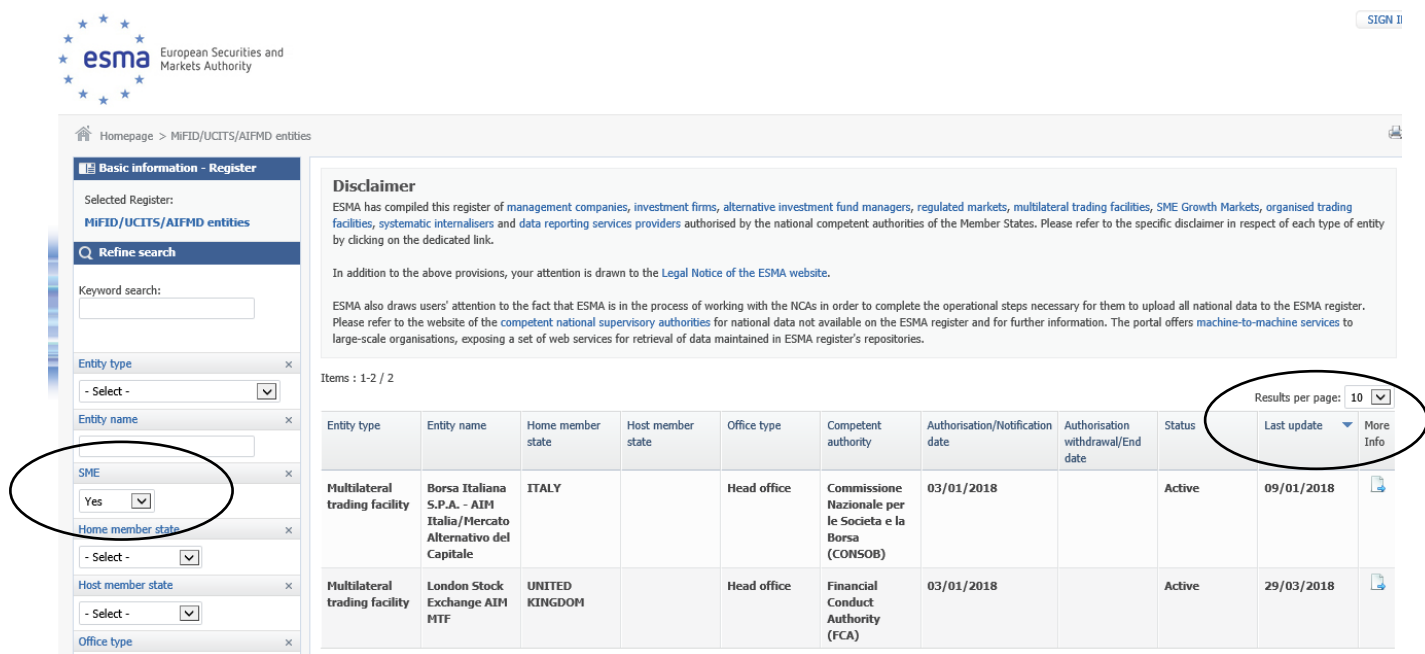
Use file: "MiFID II/MiFIR TV/SI/DRSP" to open:

https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_upreg

Considering the attached screenshot:

- set filter in selection field "SME" to "YES";
- in order to see the MIC[30], the detailed view "More Info" must be opened.



---

[30] As of 24.05.2019, four venues qualified as SME Growth Markets; the relevant MICs are: XAIM, AIMX, GBUL, XZAP.

## 5.6 INSTRUMENT CATEGORY PENALTY RATE

Considering all the previously mentioned decision criteria, CSDs shall apply the ESMA penalty rates as quoted below and published as such in the Delegated Regulation 2017/389[31]:

| Type of fail | Rate |
|---|---|
| 1. Settlement fail due to **a lack of shares that have a liquid market** within the meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014, excluding shares referred to in point 3 | 1,0 basis point |
| 2. Settlement fail due to **a lack of shares that do not have a liquid market** within the meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014, excluding shares referred to in point 3 | 0,5 basis point |
| 3. Settlement fail due to a **lack of financial instruments traded on SME growth markets**, excluding debt instruments referred to in point 6 | 0,25 basis point |

---

[31] European Commission Delegated Regulation (EU) 2017/389, of 11 November 2016, supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council as regards the parameters for the calculation of cash penalties for settlement fails and the operations of CSDs in host Member States. Published at: http://eur-lex.europa.eu/eli/reg_del/2017/389/oj When applicable, updates are expected to be provided by ESMA.

| | |
|---|---|
| 4. Settlement fail due to a **lack of debt instruments** issued or guaranteed by:<br><br>  (a)   a sovereign issuer as defined in Article 4(1)(60) of Directive 2014/65/EU;<br><br>  (b)   a third country sovereign issuer;<br><br>  (c)   a local government authority;<br><br>  (d)   a central bank;<br><br>  (e)   any multilateral development bank referred to in the second subparagraph of Article 117(1) and in Article 117(2) of Regulation (EU) No 575/2013 of the European Parliament and of the Council (¹);<br><br>  (f)   the European Financial Stability Facility or the European Stability Mechanism. | 0,10 basis point |
| 5. Settlement fail due to a **lack of debt instruments other** than those referred to in points 4 and 6 | 0,20 basis point |
| 6. Settlement fail due to a **lack of debt instruments traded on SME growth markets** | 0,15 basis point |
| 7. Settlement fail due to a **lack of all other financial instruments** not covered in points 1 to 6 | 0,5 basis point |
| 8. Settlement fail due to a **lack of cash** | Official interest rate for overnight credit charged by the central bank issuing the settlement currency with a floor of 0 (zero)[32] |

## 5.7 CENTRAL BANK DISCOUNT RATE (PENALTIES DUE TO LACK OF CASH)

CSDs must source the relevant interest rate for the currency of the failing settlement instruction in case the fail reason is "lack of cash".

---

[32] As this is an annual rate, a conversion to a "daily rate" shall be applied for penalties the calculations (see Chapter 5.7).

The cash discount rate is the official interest rate of the central bank issuing the settlement currency that should evidence the borrowing costs for that currency.

For Euro, this is the "marginal lending facility rate" which is published on the ECB website[33].

[ESMA to officially confirm:] For penalties calculations, the annual cash discount rate shall be divided by 365 days in order to generate the applicable daily penalty rate.

ECSDA is considering to collect and maintain a list of discount rates per currency from the Central Banks´ websites.

## 5.8 FOREIGN EXCHANGE RATES (FX)

For non-EUR currencies, the relevant Central Banks' Foreign exchange (FX) rates shall be consulted.

As explained in Chapter 6, for FOP instructions related penalties, a FX conversion to another currency may be required.

CSDs must then source the relevant FX rate for the relevant currency of the failing settlement instruction (for EUR, various FX rates are published by ECB on their website[34]; in case FX rates are missing or other cross-rates (e.g. SEK/ DKK) are needed, these must be sourced by CSDs preferably from the respective National Central Bank issuing the currency).

---

[33] Discount rates would be updated by the corresponding to the currency EU Central Banks. For the ECB rates, please see http://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html.http://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html.http://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html.http://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html

[34] http://www.ecb.europa.eu/stats/exchange/eurofxref/html/index.en.html

# 6 PENALTIES CURRENCIES CONVERSIONS NEEDS

This chapter suggests an approach for scenarios involving multiple CSDs, when the currency of the reference price or cash penalty is calculated in a currency that is not eligible at an involved CSD. As it is the responsibility of the CSD being a participant to the Calculating CSD to ensure the payment is executed towards the Calculating CSD in the currency as reported, the handling of a potential cash conversion is ultimately left to the discretion of the CSD.

In an intra-CSD context, the currency to be used for the penalties is at the discretion of the CSD; however, for DVP instructions, the currency of the cash leg should be applied.

An issue related to the penalties collections/ redistribution due to divergent currencies can materialise only in a <u>free of payment</u>[35] settlement fails scenario where the penalty currency applied by the Calculating CSD is not eligible in the other CSD(s) or settlement platform (e.g. T2S). CSD participants may be required to arrange FX transactions in the payment month, considering the timelines described in chapter 2.

Generally, the instrument reference price currency shall be applied by the Calculating CSD and the other CSD(s) involved in the settlement, i.e. the amount imposed by the penalty shall be calculated in one of the following ways:

a) either the denomination currency of the underlying security, if the instrument is quoted in nominal or per cent (usually fixed Income instruments); or
b) the currency of the daily reference price, if the underlying security is quoted in units (usually shares).

I**f a currency is not eligible at the Calculating CSD** (i.e. settlement or cash accounts in the reported currency are not available for participants), a currency conversion process shall apply by the Calculating CSD (using a default currency to be defined by the CSD) as follows:

1. converts the reference price into a price in the CSD´s default currency;
2. calculates the penalty amount in the default currency and rounds the amount up at least to the first two decimals;
3. per CSD, currency and party, reports the penalty amount and FX rate applied on the reference price in the daily penalty reporting.

The Calculating CSD subsequently reflects the amount in its monthly reports and payment pre-advices (if applicable). Note that no cash is actually to be exchanged on a daily basis but payments are only made once a month.

<u>Cross-CSD settlement fails</u>

---

[35] For against payment transactions, by definition, the settlement currency must be eligible in all CSDs involved in the settlement; this applies for intra- and cross-CSD settlements. In case the reference price is deviating from the currency of the cash leg, conversion into the settlement currency must be applied by the penalties Calculating CSD. In case of fails due to lack of cash, the penalty amount shall always be calculated in the currency of the cash leg.

**OPEN ITEM ECSDA:** It is yet to be discussed how the Calculating CSD can be paid by the Investor-CSD (or the Investor-CSD by its underlying participants) in case the Investor-CSD does not offer cash accounts/ settlement in the currency applied by the Calculating CSD.

As described before, the penalty currency(ies) to be processed is defined by the Calculating CSD. Subsequently, Investor-CSDs should collect from/ pay to its clients in the currency as reported by the Calculating CSD in order to avoid that FX exposures to occur on the level of the Investor-CSDs.

Hence, the Investor-CSD(s) being participants of the Calculating CSD, shall process the following reporting, representing the currency(ies) as applied by the Calculating CSD:

1. the daily reporting of penalties;
2. the monthly aggregated reporting of penalties over the calculation period per currency and party;
3. the aggregated amounts to be collected/ redistributed per currency and party.

After reception from the Calculating CSD, the Investor-CSD reports the penalties further to its underlying participants and secures the collection/ distribution of the penalty amounts on a monthly basis in each currency as reported by the Calculating CSD.

As the monthly penalty amounts due represent the sums of the daily calculated amounts with the actual cash provision being required only once by the 17th business day of the month, CSDs or their participants are not deemed to be subject to any FX exposure risks.

# 7 CALCULATION METHODS OF THE CASH PENALTIES

As also described in chapter 9, the (obligation for the) calculation of penalties depends on the settlement platform:

- for T2S, as the T2S penalty mechanism knows both, the receipt and delivery leg of the transaction, the involved CSDs can rely on T2S to calculate the penalties.

- for intra-CSD settlements outside T2S, the CSD on whose platform settlement takes place is calculating the penalties.

- For non-T2S cross-CSD settlements, the (Issuer-)CSD where the ultimate settlement takes place calculates the penalties for both legs of the transaction.

- For Bridge settlement, the delivering CSD performs the calculation.

As a general rule, all penalty amounts shall be rounded up by CSDs at least to the first two decimals.

Note re. partially successful buy-ins:

CSDR RTS Article 16.3[36] (referring to Art. 27.10 (c), 29.11 (b) and 31.11 (b)) stipulates that cash penalties shall apply to new settlement instructions resulting from a partially successful buy-in (i.e. representing the remaining part of the transaction that could not be bought in) only as of the date of entry into the CSD system (i.e. not from the ISD).

In order for CSDs to be able to comply with this requirement, the relevant CSD participants (including CCPs) should apply a market practice in such instances, requesting them to provide a specific qualifier in their settlement instructions; otherwise, CSDs cannot ensure the avoidance of LMFP calculations on an automated basis:

ISO15022/ MT54x: instructions must contain in sequence B "Trade Details", field 22F::RPOR//BYIY[37].

ISO20022: "Trade Detail/ Reporting/BYIY" (see e.g. sese.023).

Note: only when these values are present on both, the receipt and delivery instruction, LMFP would not be applied under this exemption rule.

Alternatively, CSD participants may adapt the ISD for such new instructions to a later date.

---

[36] "(…) *Where new settlement instructions are entered into the securities settlement system for any non-delivered financial instruments in accordance with Article 27(10), Article 29(11) or Article 31(11)* [these Articles refer to partial buy-ins], *cash penalties shall apply to the new settlement instructions from the day those instructions are entered into the securities settlement system.*"

[37] The differentiation to the buy-in instruction using the same BYIY code is made by the qualifier ("22F:: SETR// BYIY" vs. "RPOR//BYIY").

## 7.1 SETTLEMENT FAIL PENALTY (SEFP)

Once a failing settlement instruction has been identified as subject to computation of SEFP according to the detection rules described in chapter 3 and it was determined that a penalty is imposed (refer to chapter 4), the CSD can calculate the penalty to be applied.

The amount imposed by the penalty must be calculated depending on: (i) the type of transaction formed by the two matched settlement instructions using reference data, (ii) penalty rate of the ISIN or discount rate (Central Bank interest rate on cash) for the financial instrument exchanged by the transaction and (iii) whether the instruments need to be delivered or received by the counterparty.

It is to be noted that:

- when a settlement fail reason "lack of securities" has been identified by the CSD, no additional fail check for a "lack of cash" shall be made by the CSD.
- for currencies aspects, please refer to chapter 6.for various calculation examples, please refer to the T2S Penalty Mechanism document (see Annex "Annex I- T2S documents").

The following table summarises the basis for calculating the penalty amount for each type of transaction:

| Type of transaction | SEFP |
|---|---|
| - Delivering versus Payment (DVP) <br> -- Delivering Free of Payment (DFP) <br> - Receiving Free of Payment (RFP) | Penalty based on the quantity of securities failed to be delivered and Security penalty rate of the relevant asset type[38]. |
| - Receiving versus Payment (RVP) | Penalty based on the quantity of securities failed to be delivered and the discount rate of the relevant currency. |
| - Debiting Payment Free of Delivery (DPFOD) <br> - Crediting Payment Free of Delivery (CPFOD) | Penalty based on the amount of cash failed to be delivered and the discount rate of the relevant currency. |
| - Delivering with Payment (DWP) <br> - Receiving with Payment (RWP) | Penalty will be the sum of: <br> - Penalty based on the quantity of securities failed to be delivered and Security penalty rate of the relevant asset type; and <br> - Penalty based on the amount of cash failed to be delivered and the discount rate of the currency. |

*Note: if a fail is due to an instruction which is put on hold, such instruction on hold is to be considered as the failing one, and the above-mentioned formulas have to be applied.*

---

38 Penalty rate as determined in the Delegated Act where the penalty rates have been set.

The formulas to calculate the penalty imposed by a Settlement Fail Penalty (SEFP) are the following:

- **i. For a failing DVP, DFP or RFP Settlement Instruction (including when on hold):**

  SEFP = Security Penalty Rate*Reference Price*Quantity

  - **Security Penalty Rate** is the penalty rate stored in Static Data for the relevant asset type (derived from the ISIN and Place of trade) and the business day for which the penalty is calculated;

  - **Reference Price** is the price stored in static data for the ISIN of the instruction and the business day for which the penalty is calculated;

  - **Quantity** is the quantity of securities failed to be delivered, which is the quantity of the instruction remaining to be settled at the time of end of processing of the relevant cut-off.

- **ii. For a failing RVP Settlement Instruction (including when on hold):**

  SEFP = Cash Discount Penalty Rate*Reference Price*Quantity

  - **Cash Discount Penalty Rate** is the discount rate of the relevant currency stored in Static Data divided by 365 and the business day for which the penalty is calculated.

  - **Reference Price** is the price stored in Static Data for the ISIN of the instruction and the business day for which the penalty is calculated.

  - **Quantity** is the quantity of securities failed to be delivered, which is the quantity of the instruction remaining to be settled at the time of end of processing of the relevant cut-off.

- **iii. For a failing DPFOD or CPFOD Settlement Instruction (including when on hold):**

  SEFP = Cash Discount Penalty Rate*Amount

  - **Cash Discount Penalty Rate** is the discount rate of the relevant currency stored in Static Data divided by 365 and the business day for which the penalty is calculated.

  - **Amount** is the cash amount failed to be delivered, which is the amount of the instruction remaining to be settled at the time of end of processing of the relevant cut-off[39].

- **iv. For a failing DWP or RWP Settlement Instruction (including when on hold):**

  SEFP = Security Penalty Rate* Reference Price* Quantity + Cash Discount Penalty Rate* Amount

---

[39] Rationale: Although the CSDR prescribes to use the security quantity and reference price for the calculation of all settlement fail penalties, for DPFOD and CPFOD settlement instructions where the ISIN quantity is 0, the assumption is to use the cash amount to compute the penalty.

- Security Penalty Rate**Reference Price**Quantity as described in (i);

- Cash Discount Penalty Rate** Amount as described in (iii).

*Note 1: the penalties amounts might be reported with various decimals, but the monthly payment amounts shall be rounded up at least to the first two decimals.*

## 7.2 *NOTE 2: THE PENALTIES CALCULATED SHOULD BE RETAINED FOR 3 MONTHS.* LATE MATCHING FAIL PENALTY (LMFP)

For settlement instructions that are matched in the CSD system only after the relevant cut-off of their Intended Settlement Date (ISD), penalties shall be calculated only once (i.e. on the business day when they are matched) but considering all the <u>previous</u> business days where the instruction failed to settle due to the late matching[40].

Settlement Fail Penalties (SEFP) and Late Matching Fail Penalties (LMFP) shall follow the same principles for their computation.

### 7.2.1 Number of days considered in the computation of LMFP

The number of days to consider in the formula to calculate the amount imposed by a Late Matching Fail Penalty (LMFP) will differ depending on whether the instruction subject to LMFP can either still settle, or no longer settle, on the business day when the instruction is matched (i.e. depending on whether it is matched before or after the relevant cut-off for the Matching Business Day).

1. **When the instruction can still settle on the business day when it is matched:**

   - This scenario relates to those instructions matched after their ISD (late matching) but matched at a point in time when it is still possible to settle them on the business day when they are matched (i.e. matched before the relevant cut-off for Matching Business day).

   - The LMFP shall be calculated for each business day as from the ISD until, and excluding, the business day when the instruction is matched.

   - In case the instruction does not settle on the business day when it is matched (even if it was possible because it arrived before the cut-off) then, a separate calculation will have to be performed for an additional SEFP.

---

[40] Amendments could still be performed on these LMFP, in case of reference data updates for instance.
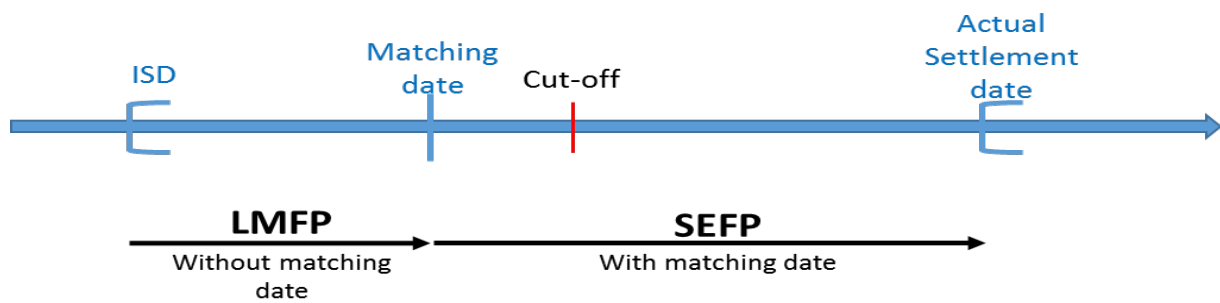
The matching date is excluded from the LMFP and included in the SEFP.

2. **When the instruction can no longer settle on the business day when it is matched:**

- This scenario relates to those instructions matched, on or after the ISD, at a point in time when it is not possible to settle them on the business day when they are matched, because it is after the relevant cut-off.

- The LMFP shall be calculated for each business day as from the ISD until, and including, the business day when the instruction is matched.
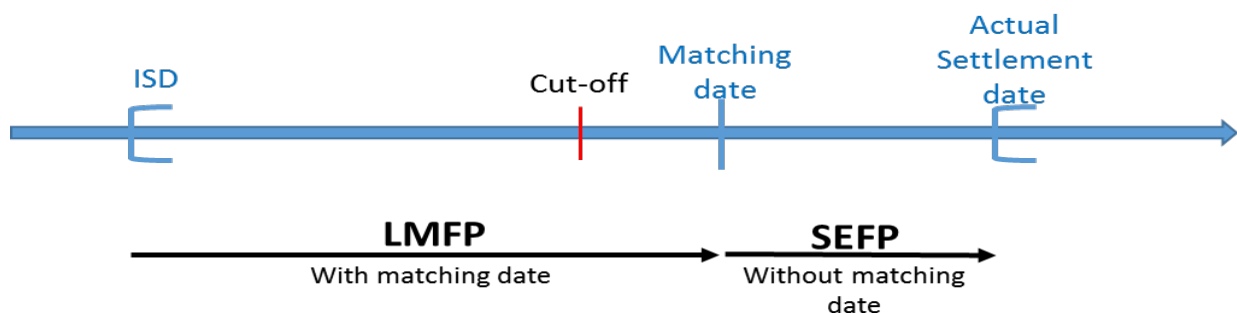


The matching date is included in the LMFP and excluded from the SEFP.

### 7.2.2    Formulas to be used

Note: Everything will be the same as for instructions that can still settle but, additionally, the business day when the instructions are matched must be included.

**i. For a DVP, DFP or RFP received late:**

LMFP = Security Penalty Rate*Reference Price*Quantity

- **Security Penalty Rate** is the penalty rate stored in Static Data for the relevant asset type (derived from the ISIN and Place of trade) and for the relevant business day.

- **Reference Price** is the price stored in Static Data for the ISIN of the instruction and for the relevant business day.

- **Quantity** is the quantity of securities failed to be delivered, which is the matched quantity of the Settlement Instruction.

**ii. For a RVP received late:**

LMFP = Cash Discount Penalty Rate**\*** Reference Price**\*** Quantity, where;

- **Cash Discount Penalty Rate** is the discount rate of the relevant currency stored in Static Data divided by 365 and the business day for which the penalty is calculated;

- **Reference Price** is the price stored in Static Data for the ISIN of the instruction and the relevant business day.

- **Quantity** is the quantity of securities failed to be delivered, which is the matched quantity of the instruction.

### iii. For a RVP received late and as an already matched instruction:

LMFP = Security Penalty Rate **\*** Reference Price**\*** Quantity, where:

- **Security Penalty Rate** is the penalty rate stored in Static Data for the relevant asset type (derived from the ISIN and Place of trade) and for the relevant business day;

- **Reference Price** is the price stored in Static Data for the ISIN of the instruction and the relevant business day**;**

- **Quantity** is the quantity of securities failed to be delivered, which is the matched quantity of the instruction.

### iv. For a DPFOD or CPFOD received late (ISIN quantity is 0):

- LMFP = Cash Discount Penalty Rate**\*** Amount;
- **Cash Discount Penalty Rate** is the discount rate of the relevant currency stored in Static Data divided by 365 for the relevant business day;
- **Amount** is the cash amount failed to be delivered, which is the matched cash amount of the Settlement Instruction.

### v. For a DWP or RWP received late:

- LMFP = Security Penalty Rate **\*** Reference Price **\*** Quantity + Cash Discount Penalty Rate **\*** Amount;

- Security Penalty Rate**\***Reference Price**\***Quantity as described in (i);

- Cash Discount Penalty Rate**\*** Amount as described in (iv).


## 7.3   *NOTE: THE PENALTIES CALCULATED SHOULD BE RETAINED FOR 3 MONTHS. DAILY BILATERAL NET PER COUNTERPARTY*

In addition to the gross penalties calculated on a daily basis, a bilateral net amount per CSD (only relevant for cross-CSD fails), per currency and counterparty must be provided.

For each relevant business day, a net amount is calculated for the party against each of its counterparties.

Thus, for a given party, the bilateral net amount (due or entitled) against a given counterparty is:

- The sum of all the penalties (SEFP + LMFP) calculated at the failed instruction level that this party is entitled to receive (reported as credit) from a given counterparty (i.e. to be paid by this counterpart) in a CSD;

minus

- The sum of all the penalties (SEFP + LMFP) calculated at the failed instruction level that are imposed to the party (reported as debit) and to be paid to the same counterparty in the same CSD.

If the result is a positive amount, the bilateral net amount will be a credit for the party (i.e. an amount entitled from the counterpart) and if the result is a negative amount, the bilateral net amount will be a debit (i.e. an amount due to the counterpart).

Note: No netting is to be performed across CSDs and currencies, i.e. a net by CSD, currency and counterparty must be applied.

*Example of daily bilateral (net) amounts aggregation:*

**Gross penalties calculated on a daily basis:**

|  | CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|---|---|---|---|---|---|---|---|
| Inx 1 | I | A | I | B | EUR | -100 | Intra-CSD |
| Inx 1 | I | B | I | A | EUR | +100 | Intra-CSD |
| Inx 2 | I | A | I | B | EUR | +50 | Intra-CSD |
| Inx 2 | I | B | I | A | EUR | -50 | Intra-CSD |
| Inx 3 | I | A | I | C | EUR | -20 | Intra-CSD |
| Inx 3 | I | C | I | A | EUR | +20 | Intra-CSD |
| Inx 4 | I | A | I | C | DKK | +10 | Intra-CSD |
| Inx 4 | I | C | I | A | DKK | -10 | Intra-CSD |
| Inx 5 | I | A | II | Unknown | DKK | -10 | Cross-CSD (PSET CSD I) |
| Inx 5 | II | B | I | A | DKK | +10 | Cross-CSD (PSET CSD I) |
| Inx 6 | I | A | II | Unknown | DKK | +20 | Cross-CSD (PSET CSD I) |
| Inx 6 | II | B | I | A | DKK | -20 | Cross-CSD (PSET CSD I) |
| Inx 7 | I | B | I | A | EUR | +150 | Intra-CSD |
| Inx 7 | I | A | I | B | EUR | -150 | Intra-CSD |
| Inx 8 | I | B | I | C | EUR | -25 | Intra-CSD |
| Inx 8 | I | C | I | B | EUR | +25 | Intra-CSD |
| Inx 9 | I | C | II | B | EUR | +250 | Cross-CSD (PSET CSD II) |
| Inx 9 | II | B | I | Unknown | EUR | -250 | Cross-CSD (PSET CSD II) |
| Inx 10 | I | C | II | D | EUR | -300 | Cross-CSD (PSET CSD II) |
| Inx 10 | II | D | I | Unknown | EUR | +300 | Cross-CSD (PSET CSD II) |
| Inx 11 | I | A | I | A | DKK | +625 | Intra-CSD |
| Inx 11 | I | A | I | A | DKK | -625 | Intra-CSD |

| Inx 12 | I | B | III | Unknown | EUR | +28 | Cross-CSD (PSET CSD I) |
|--------|---|---|-----|---------|-----|-----|------------------------|
| Inx 12 | III | C | I | B | EUR | -28 | Cross-CSD (PSET CSD I) |
| Inx 13 | I | B | III | B | EUR | -49 | Cross-CSD (PSET CSD III) |
| Inx 13 | III | B | I | Unknown | EUR | +49 | Cross-CSD (PSET CSD III) |
| Inx 14 | I | A | II | C | DKK | +23 | Cross-CSD (PSET II) |
| Inx 14 | II | C | I | Unknown | DKK | -23 | Cross-CSD (PSET II) |

**Daily bilateral net amount per CSD, per currency & per counterparty (view per CSD participant):**

For party A in CSD I:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|-----|-------|-----|--------------|----------|-----------|---------|
| I | A | I | B | EUR | -200 | Intra-CSD |
| I | A | I | C | EUR | -20 | Intra-CSD |
| I | A | I | C | DKK | +10 | Intra-CSD |
| I | A | II | Unknown | DKK | +10 | Cross-CSD (PSET CSD I) |
| I | A | I | A | DKK | 0 | Intra-CSD |
| I | A | II | C | DKK | +23 | Cross-CSD (PSET II) |

For party B in CSD I:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|-----|-------|-----|--------------|----------|-----------|---------|
| I | B | I | A | EUR | +200 | Intra-CSD |
| I | B | I | C | EUR | -25 | Intra-CSD |
| I | B | III | Unknown | EUR | +28 | Cross-CSD (PSET CSD I) |
| I | B | III | B | EUR | -49 | Cross-CSD (PSET CSD III) |

For party B in CSD II:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|-----|-------|-----|--------------|----------|-----------|---------|
| II | B | I | A | DKK | -10 | Cross-CSD (PSET CSD I) |
| II | B | I | Unknown | EUR | -250 | Cross-CSD (PSET CSD II) |

For party B in CSD III:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|-----|-------|-----|--------------|----------|-----------|---------|
| III | B | I | Unknown | EUR | +49 | Cross-CSD (PSET CSD III) |

For party C in CSD I:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|-----|-------|-----|--------------|----------|-----------|---------|
| I | C | I | A | EUR | +20 | Intra-CSD |
| I | C | I | A | DKK | -10 | Intra-CSD |
| I | C | I | B | EUR | +25 | Intra-CSD |

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|---|---|---|---|---|---|---|
| I | C | II | B | EUR | +250 | Cross-CSD (PSET CSD II) |
| I | C | II | D | EUR | -300 | Cross-CSD (PSET CSD II) |

For party C in CSD II:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|---|---|---|---|---|---|---|
| II | C | I | Unknown | DKK | -23 | Cross-CSD (PSET II) |

For party C in CSD III:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|---|---|---|---|---|---|---|
| III | C | I | B | EUR | -28 | Cross-CSD (PSET CSD I) |

For party D in CSD II:

| CSD | Party | CSD | Counterparty | Currency | Penalties | Comment |
|---|---|---|---|---|---|---|
| II | D | I | Unknown | EUR | +300 | Cross-CSD (PSET CSD II) |


**Daily bilateral net amount per CSD, per currency & per counterparty (view per CSD):**

CSD I:

| CSD | CSD | Currency | Penalties | Comment |
|---|---|---|---|---|
| I | I | EUR | 0 | Intra-CSD |
| I | I | DKK | 0 | Intra-CSD |
| I | II | EUR | -50 | Cross-CSD (PSET CSD II) |
| I | II | DKK | +10 | Cross-CSD (PSET CSD I) |
| I | II | DKK | +23 | Cross-CSD (PSET II) |
| I | III | EUR | +28 | Cross-CSD (PSET CSD I) |
| I | III | EUR | -49 | Cross-CSD (PSET CSD III) |

CSD II:

| CSD | CSD | Currency | Penalties | Comment |
|---|---|---|---|---|
| II | I | DKK | -10 | Cross-CSD (PSET CSD I) |
| II | I | DKK | -23 | Cross-CSD (PSET II) |
| II | I | EUR | +50 | Cross-CSD (PSET CSD II) |

CSD III:

| CSD | CSD | Currency | Penalties | Comment |
|---|---|---|---|---|
| III | I | EUR | +49 | Cross-CSD (PSET CSD III) |
| III | I | EUR | -28 | Cross-CSD (PSET CSD I) |

## 7.4 MONTHLY CASH PENALTIES AGGREGATION AND GLOBAL NET AMOUNTS

### 7.4.1 Monthly bilateral net per counterparty

On the 14th business day of the month, bilateral net amounts of the penalties computed for all the business days of the previous month is calculated per CSD, currency and party against each of its counterparties.

When calculating the monthly aggregated amounts, the CSD will consider the last available value of the amount of each penalty aggregated (i.e. the CSD will take into account all the modifications performed until the end of the penalties appeal period for CSDs, i.e. changes until and including the 11th business day of the following month).

This **aggregation** of the monthly penalties per CSD[41], currency and counterparty (i.e. bilateral net amounts) allows to:

- Isolate the amounts of the CCPs that shall not be collected and re-distributed by the CSD;
- Isolate non-payments from CSD participants (i.e. participants affected by a non-payment of its counterpart as well as the amount that cannot be distributed by the CSD since it was not collected could be easily identified);
- Provide a netting as required by the CSDR;
- Reduce the required liquidity.

Accordingly, for each CSD, party and currency, the monthly bilateral net amount equals to:

- The sum of all the cash penalties of the previous month in the relevant currency, that the party is entitled to receive (reported as credit) from a given counterparty (i.e. to be paid by this counterparty);

Minus

- The sum of all the cash penalties of the previous month in the relevant currency and that were imposed to the party (reported as debit), and to be paid to the same counterparty.

Subsequently, for each party of a CSD, a "net amount per counterparty" is calculated.

If the result is a positive amount, the bilateral net amount will be a credit for the party (i.e. an amount entitled to be received from the counterpart) and if the result is a negative amount, the bilateral net amount will be a debit (i.e. an amount due to the counterpart).

*Example: Monthly cash penalties aggregation (non-T2S cross-CSD settlement fails)*

**Daily bilateral amounts of the business days of the month:**

| BD | CSD | Party | CSD | Cpty | Curr. | Penalties | Comment |
|----|-----|-------|-----|------|-------|-----------|---------|

---

[41] This means, that penalties amounts cannot be netted ("mixed") between CSDs in scenarios where CSD A is Investor-CSD at Issuer-CSD B and CSD B is Investor-CSD at Issuer-CSD A.

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Day 1 | I | A | I | B | EUR | -200 | Intra-CSD |
| Day 1 | I | B | I | A | EUR | +200 | Intra-CSD |
| Day 1 | I | A | I | C | EUR | -20 | Intra-CSD |
| Day 1 | I | C | I | A | EUR | +20 | Intra-CSD |
| Day 1 | I | A | I | C | DKK | +10 | Intra-CSD |
| Day 1 | I | C | I | A | DKK | -10 | Intra-CSD |
| Day 1 | I | A | II | Unknown | DKK | +10 | Cross-CSD (PSET CSD I) |
| Day 1 | II | B | I | A | DKK | -10 | Cross-CSD (PSET CSD I) |
| Day 1 | I | A | I | A | DKK | 0 | Intra-CSD |
| Day 1 | I | A | II | C | DKK | +23 | Cross-CSD (PSET II) |
| Day 1 | II | C | I | Unknown | DKK | -23 | Cross-CSD (PSET II) |
| Day 1 | I | B | I | C | EUR | -25 | Intra-CSD |
| Day 1 | I | C | I | B | EUR | +25 | Intra-CSD |
| Day 1 | I | B | III | Unknown | EUR | +28 | Cross-CSD (PSET CSD I) |
| Day 1 | III | C | I | B | EUR | -28 | Cross-CSD (PSET CSD I) |
| Day 1 | I | B | III | B | EUR | -49 | Cross-CSD (PSET CSD III) |
| Day 1 | III | B | I | Unknown | EUR | +49 | Cross-CSD (PSET CSD III) |
| Day 1 | II | B | I | Unknown | EUR | -250 | Cross-CSD (PSET CSD II) |
| Day 1 | I | C | II | B | EUR | +250 | Cross-CSD (PSET CSD II) |
| Day 1 | I | C | II | D | EUR | -300 | Cross-CSD (PSET CSD II) |
| Day 1 | II | D | I | Unknown | EUR | +300 | Cross-CSD (PSET CSD II) |
| Day 3 | I | A | I | D | EUR | -200 | Intra-CSD |
| Day 3 | I | D | I | A | EUR | +200 | Intra-CSD |
| Day 3 | I | A | II | Unknown | DKK | -23 | Cross-CSD (PSET CSD I) |
| Day 3 | II | B | I | A | DKK | +23 | Cross-CSD (PSET CSD I) |
| Day 3 | I | B | I | C | EUR | +18 | Intra-CSD |
| Day 3 | I | C | I | B | EUR | -18 | Intra-CSD |
| Day 3 | I | B | III | Unknown | EUR | -62 | Cross-CSD (PSET CSD I) |
| Day 3 | III | B | I | B | EUR | +62 | Cross-CSD (PSET CSD I) |
| Day 3 | I | C | II | D | EUR | -300 | Cross-CSD (PSET CSD II) |
| Day 3 | II | D | I | Unknown | EUR | +300 | Cross-CSD (PSET CSD II) |
| Day 5 | I | A | I | C | DKK | +10 | Intra-CSD |
| Day 5 | I | C | I | A | DKK | -10 | Intra-CSD |
| Day 5 | I | B | I | A | EUR | -47 | Intra-CSD |
| Day 5 | I | A | I | B | EUR | +47 | Intra-CSD |
| Day 10 | I | A | I | B | EUR | +2500 | Intra-CSD |
| Day 10 | I | B | I | A | EUR | -2500 | Intra-CSD |
| Day 10 | I | A | I | C | EUR | -480 | Intra-CSD |

| Day | | CSD | Cpty | Curr | Amount | Comment |
|---|---|---|---|---|---|---|
| Day 10 | I | C | I | A | EUR | +480 | Intra-CSD |
| Day 10 | I | A | I | C | DKK | +67 | Intra-CSD |
| Day 10 | I | C | I | A | DKK | -67 | Intra-CSD |
| Day 10 | I | A | II | Unknown | DKK | -19 | Cross-CSD (PSET CSD I) |
| Day 10 | II | B | I | A | DKK | +52 | Cross-CSD (PSET CSD I) |
| Day 10 | II | D | I | A | DKK | -33 | Cross-CSD (PSET CSD I) |
| Day 10 | I | A | I | A | DKK | 0 | Intra-CSD |
| Day 10 | I | A | II | C | DKK | -857 | Cross-CSD (PSET CSD II) |
| Day 10 | II | C | I | Unknown | DKK | +857 | Cross-CSD (PSET CSD II) |
| Day 10 | I | B | III | Unknown | EUR | +2368 | Cross-CSD (PSET CSD I) |
| Day 10 | III | B | I | B | EUR | -2368 | Cross-CSD (PSET CSD I) |
| Day 10 | I | B | III | B | EUR | -56 | Cross-CSD (PSET CSD III) |
| Day 10 | III | B | I | Unknown | EUR | +56 | Cross-CSD (PSET CSD III) |
| Day 10 | I | C | II | A | EUR | -475 | Cross-CSD (PSET CSD II) |
| Day 10 | II | A | I | Unknown | EUR | +475 | Cross-CSD (PSET CSD II) |
| Day 10 | I | C | II | B | EUR | -587 | Cross-CSD (PSET CSD II) |
| Day 10 | II | B | I | Unknown | EUR | +587 | Cross-CSD (PSET CSD II) |
| Day 15 | I | A | II | D | DKK | +70 | Cross-CSD (PSET CSD II) |
| Day 15 | I | B | II | D | DKK | -45 | Cross-CSD (PSET CSD II) |
| Day 15 | II | D | I | Unknown | DKK | -25 | Cross-CSD (PSET CSD II) |
| Day 15 | I | A | I | D | EUR | -65 | Intra-CSD |
| Day 15 | I | D | I | A | EUR | +65 | Intra-CSD |
| Day 15 | I | A | I | B | EUR | +100 | Intra-CSD |
| Day 15 | I | B | I | A | EUR | -100 | Intra-CSD |
| Day 22 | I | A | I | C | EUR | +20 | Intra-CSD |
| Day 22 | I | C | I | A | EUR | -20 | Intra-CSD |
| Day 22 | I | A | II | B | DKK | -50 | Cross-CSD (PSET CSD II) |
| Day 22 | II | B | I | Unknown | DKK | +50 | Cross-CSD (PSET CSD II) |
| Day 22 | I | A | II | Unknown | EUR | -356 | Cross-CSD (PSET CSD I) |
| Day 22 | II | D | I | A | EUR | +356 | Cross-CSD (PSET CSD I) |

**Monthly bilateral net amount per CSD, per currency & per counterparty (view per CSD participant):**

For party A in CSD I:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| I | A | I | B | EUR | +2447 | Intra-CSD |
| I | A | I | C | EUR | -480 | Intra-CSD |

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| I | A | I | C | DKK | +87 | Intra-CSD |
| I | A | II | Unknown | DKK | -32 | Cross-CSD (PSET CSD I) |
| I | A | I | A | DKK | 0 | Intra-CSD |
| I | A | II | C | DKK | -834 | Cross-CSD (PSET CSD II) |
| I | A | I | D | EUR | -265 | Intra-CSD |
| I | A | II | D | DKK | +70 | Cross-CSD (PSET CSD II) |
| I | A | II | B | DKK | -50 | Cross-CSD (PSET CSD II) |
| I | A | II | Unknown | EUR | -356 | Cross-CSD (PSET CSD I) |

For party A in CSD II:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| II | A | I | Unknown | EUR | +475 | Cross-CSD (PSET CSD II) |

For party B in CSD I:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| I | B | I | A | EUR | -2447 | Intra-CSD |
| I | B | I | C | EUR | -7 | Intra-CSD |
| I | B | III | Unknown | EUR | +2334 | Cross-CSD (PSET CSD I) |
| I | B | III | B | EUR | -105 | Cross-CSD (PSET CSD III) |
| I | B | II | D | DKK | -45 | Cross-CSD (PSET CSD II) |

For party B in CSD II:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| II | B | I | A | DKK | +65 | Cross-CSD (PSET CSD I) |
| II | B | I | Unknown | EUR | +337 | Cross-CSD (PSET CSD II) |
| II | B | I | Unknown | DKK | +50 | Cross-CSD (PSET CSD II) |

For party B in CSD III:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| III | B | I | Unknown | EUR | +105 | Cross-CSD (PSET CSD III) |
| III | B | I | B | EUR | -2306 | Cross-CSD (PSET CSD I) |

For party C in CSD I:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|---|---|---|---|---|---|---|
| I | C | I | A | EUR | +480 | Intra-CSD |
| I | C | I | A | DKK | -87 | Intra-CSD |
| I | C | I | B | EUR | +7 | Intra-CSD |
| I | C | II | B | EUR | -337 | Cross-CSD (PSET CSD II) |
| I | C | II | D | EUR | -600 | Cross-CSD (PSET CSD II) |
| I | C | II | A | EUR | -475 | Cross-CSD (PSET CSD II) |

For party C in CSD II:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|-----|-------|-----|------|------|-----------|---------|
| II | C | I | Unknown | DKK | +834 | Cross-CSD (PSET CSD II) |

For party C in CSD III:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|-----|-------|-----|------|------|-----------|---------|
| III | C | I | B | EUR | -28 | Cross-CSD (PSET CSD I) |

For party D in CSD I:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|-----|-------|-----|------|------|-----------|---------|
| I | D | I | A | EUR | +265 | Intra-CSD |

For party D in CSD II:

| CSD | Party | CSD | Cpty | Curr | Penalties | Comment |
|-----|-------|-----|------|------|-----------|---------|
| II | D | I | Unknown | EUR | +600 | Cross-CSD (PSET CSD II) |
| II | D | I | A | DKK | -33 | Cross-CSD (PSET CSD I) |
| II | D | I | Unknown | DKK | -25 | Cross-CSD (PSET CSD II) |
| II | D | I | A | EUR | +356 | Cross-CSD (PSET CSD I) |

**Monthly bilateral net amount per CSD, per currency & per counterparty (view per CSD):**

CSD I:

| CSD | CSD | Curr | Penalties | Comment |
|-----|-----|------|-----------|---------|
| I | I | EUR | 0 | Intra-CSD |
| I | I | DKK | 0 | Intra-CSD |
| I | II | EUR | -356 | Cross-CSD (PSET CSD I) |
| I | II | DKK | -32 | Cross-CSD (PSET CSD I) |
| I | II | EUR | -1412 | Cross-CSD (PSET CSD II) |
| I | II | DKK | -859 | Cross-CSD (PSET CSD II) |
| I | III | EUR | +2334 | Cross-CSD (PSET CSD I) |
| I | III | EUR | -105 | Cross-CSD (PSET CSD III) |

CSD II:

| II | I | EUR | +356 | Cross-CSD (PSET CSD I) |
|----|---|-----|------|------------------------|
| II | I | EUR | +1412 | Cross-CSD (PSET CSD II) |
| II | I | DKK | +32 | Cross-CSD (PSET CSD I) |
| II | I | DKK | +859 | Cross-CSD (PSET CSD II) |

CSD III:

| CSD | CSD | Curr | Penalties | Comment |
|---|---|---|---|---|
| III | I | EUR | +105 | Cross-CSD (PSET CSD III) |
| III | I | EUR | -2334 | Cross-CSD (PSET CSD I) |

### 7.4.2 Global Net (monthly amount to be paid or to be received)

Either on the 14th business day (in case no payment pre-advice is sent) or on the 15th business day (in case of sending a payment pre-advice) of the month, a "global net amount" of the monthly nets (by counterparty) bilateral amounts are calculated per CSD and currency for each CSD party.

The date for sending this information will depend on the payment process chosen by the CSD, and the CSD's own internal process. It will be at the discretion of the CSD whether to send the global nets on the 14th BD or the 15th BD.

Accordingly, for each CSD, currency and party, the monthly net amount equals to:

- The sum of all the net bilateral amounts in the relevant currency, that the party is entitled to receive (reported as credit and for all counterparties);

Minus

- The sum of all the net bilateral amounts in the relevant currency and that were imposed to the party (reported as debit and for all counterparties).

The "global net" amount resulting from this calculation and will either be an amount due by the party (i.e. to be paid by the party), or an amount to be received by the party.

This amount will either be reported via the monthly report, a payment advice or through a PFOD instructions (the process depends on the CSD payment process and the CSD settlement platform) to the CSD participants. Please refer to chapter 11.3.3 for details.

Settlement transactions in which one party is a **CCP** will be reported by the CSD (see chapters 7.4, 12.3) but shall be excluded from the actual cash collection/ re-distribution process.

*Example of the monthly amount to be paid or to be received (non-T2S cross-CSD settlement fails):*

**Monthly amount to be paid or to be received (view per CSD participant):**

For party A in CSD I:

| CSD | Party | CSD | Curr | Penalties | Comment |
|---|---|---|---|---|---|
| I | A | I | EUR | +1702 | Intra-CSD |
| I | A | I | DKK | +87 | Intra-CSD |
| I | A | II | EUR | -356 | Cross-CSD (PSET CSD I) |
| I | A | II | DKK | -32 | Cross-CSD (PSET CSD I) |
| I | A | II | DKK | -814 | Cross-CSD (PSET CSD II) |

For party A in CSD II:

| CSD | Party | CSD | Curr | Penalties | Comment |
|---|---|---|---|---|---|
| II | A | I | EUR | +475 | Cross-CSD (PSET CSD II) |

For party B in CSD I:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| I | B | I | EUR | -2454 | Intra-CSD |
| I | B | III | EUR | +2334 | Cross-CSD (PSET CSD I) |
| I | B | II | DKK | -45 | Cross-CSD (PSET CSD II) |
| I | B | III | EUR | -105 | Cross-CSD (PSET CSD III) |

For party B in CSD II:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| II | B | I | DKK | +65 | Cross-CSD (PSET CSD I) |
| II | B | I | EUR | +337 | Cross-CSD (PSET CSD II) |
| II | B | I | DKK | +50 | Cross-CSD (PSET CSD II) |

For party B in CSD III:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| III | B | I | EUR | -2306 | Cross-CSD (PSET CSD I) |
| III | B | I | EUR | +105 | Cross-CSD (PSET CSD III) |

For party C in CSD I:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| I | C | I | EUR | +487 | Intra-CSD |
| I | C | I | DKK | -87 | Intra-CSD |
| I | C | II | EUR | -1412 | Cross-CSD (PSET CSD II) |

For party C in CSD II:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| II | C | I | DKK | +834 | Cross-CSD (PSET CSD II) |

For party C in CSD III:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| III | C | I | EUR | -28 | Cross-CSD (PSET CSD I) |

For party D in CSD I:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| I | D | I | EUR | +265 | Intra-CSD |

For party D in CSD II:

| CSD | Party | CSD | Curr | Penalties | Comment |
|-----|-------|-----|------|-----------|---------|
| II | D | I | EUR | +356 | Cross-CSD (PSET CSD I) |
| II | D | I | DKK | -33 | Cross-CSD (PSET CSD I) |

| | | | | | |
|---|---|---|---|---|---|
| II | D | I | EUR | +600 | Cross-CSD (PSET CSD II) |
| II | D | I | DKK | -25 | Cross-CSD (PSET CSD II) |

**Monthly amount to be paid or to be received (view per CSD):**

CSD I:

| CSD | CSD | Curr | Penalties | Comment |
|---|---|---|---|---|
| I | I | EUR | 0 | Intra-CSD |
| I | I | DKK | 0 | Intra-CSD |
| I | II | EUR | -356 | Cross-CSD (PSET CSD I) |
| I | II | EUR | -1412 | Cross-CSD (PSET CSD II) |
| I | II | DKK | -32 | Cross-CSD (PSET CSD I) |
| I | II | DKK | -859 | Cross-CSD (PSET CSD II) |
| I | III | EUR | +2334 | Cross-CSD (PSET CSD I) |
| I | III | EUR | -105 | Cross-CSD (PSET CSD III) |

CSD II:

| | | | | |
|---|---|---|---|---|
| II | I | EUR | +356 | Cross-CSD (PSET CSD I) |
| II | I | EUR | +1412 | Cross-CSD (PSET CSD II) |
| II | I | DKK | +32 | Cross-CSD (PSET CSD I) |
| II | I | DKK | +859 | Cross-CSD (PSET CSD II) |

CSD III:

| CSD | CSD | Curr | Penalties | Comment |
|---|---|---|---|---|
| III | I | EUR | -2334 | Cross-CSD (PSET CSD I) |
| III | I | EUR | +105 | Cross-CSD (PSET CSD III) |

As a summary, the amounts to be paid/ received are:

| Party | Pay / Receive | Curr. | Penalties | To / From | PSET |
|---|---|---|---|---|---|
| A | Receive | EUR | +1702 | CSD I | Intra-CSD |
| A | Receive | DKK | +87 | CSD I | Intra-CSD |
| B | Pay | EUR | -2454 | CSD I | Intra-CSD |
| C | Receive | EUR | +487 | CSD I | Intra-CSD |
| C | Pay | DKK | -87 | CSD I | Intra-CSD |
| D | Receive | EUR | +265 | CSD I | Intra-CSD |
| CSD I | Pay | EUR | -356 | CSD II | PSET CSD I |
| CSD I | Pay | EUR | -1412 | CSD II | PSET CSD II |

| CSD I | Receive | EUR | +2334 | CSD III | PSET CSD I |
|-------|---------|-----|-------|---------|------------|
| CSD I | Pay | EUR | -105 | CSD III | PSET CSD III |
| CSD I | Pay | DKK | -32 | CSD II | PSET CSD I |
| CSD I | Pay | DKK | -859 | CSD II | PSET CSD II |
| CSD II | Receive | EUR | +356 | CSD I | PSET CSD I |
| CSD II | Receive | EUR | +1412 | CSD I | PSET CSD II |
| CSD II | Receive | DKK | +32 | CSD I | PSET CSD I |
| CSD II | Receive | DKK | +859 | CSD I | PSET CSD II |
| CSD III | Pay | EUR | -2334 | CSD I | PSET CSD I |
| CSD III | Receive | EUR | +105 | CSD I | PSET CSD III |

# 8 CHANGES TO PREVIOUSLY CALCULATED PENALTIES

Updates of previous penalty calculations shall be done by the CSD as soon as the reference data becomes available to the CSD and considering the appeal period.

If data required for calculating penalties is available to the CSD only in the following month, retroactive penalties calculations can be made by CSDs only until the end of the 12th business day of this following month for. That means that if new or updated data for calculating penalties is available to the CSD after the 12th business day, no retroactive penalties calculations or adaptations can be made by CSDs.

Note that, in addition to the following penalties changes activities steps, T2S foresees a "switch" mechanism[42]; as this is not considered relevant for non-T2S settlements, it is not covered in this Framework.

## 8.1 REMOVAL OF EXISTING PENALTIES

In the circumstances described in Chapters 2.1.4 and 2.2.4 ("Monthly Appeal Period"), CSDs may remove an already computed and reported penalty (i.e. set the penalty amount to "zero") latest until (and including) the 11th business day of the following month.

When the removal of a penalty is performed, the CSD shall use a standard code yet to be defined with ESMA to specify the reason for the removal and provide a more detailed description why the penalty was removed, i.e. set to zero. Such information would need to be communicated to the National Competent Authorities.

The CSD shall also report the removal of a penalty in the relevant Daily Report:

- On the following business day after the removal of the penalty, the CSD shall report the removal, either in the Daily Report (with the penalties computed for the previous day), or in the report of modified penalties.

- Within this report, the penalties that have been set to zero will be reported with:

    – New amount equal to zero;

    – Status "Removed";

---

[42] Switch between the failing and non-failing party of a cash penalty: this functionality caters inter alia for cases where a transaction is settled on multiple platforms, i.e. where settlement on T2S depends on the fulfilment of a condition outside T2S. For example, when cash settlement takes place outside T2S while the settlement of securities takes place in T2S, conditional securities deliveries (CoSD) may be used by T2S Actors to block the securities in T2S until cash settlement takes place on the relevant platform. Depending on the CoSD configuration and the business scenario, T2S could compute and assign the penalty to the incorrect party (i.e. to the delivering instead of to the receiving participant or vice versa), e.g. because the free-of-payment delivery in T2S is failing, while as it is due to the lack of cash of the counterparty on the external cash settlement platform. Hence, in order to allow the CSD to make the required ex-post correction, the CSD shall be able to swap the failing party and the non-failing party of the cash penalty.

- The standard removal reason code (see Annex II); and

- Optional: a description (free text) of the reason for the removal (provided by the CSD).

## 8.2 RE-INCLUSION OF A PREVIOUSLY REMOVED PENALTY

CSDs may re-include already removed penalties as from when e.g. updated information becomes known to the CSD and latest until (and including) the 11th business day of the following month.

When a penalty is re-included, CSDs shall calculate the penalty amount again as it may have changed due to updates in the reference data since it was removed. This recalculation shall be performed by the CSD in the next CSD daily recalculation process.

CSD shall report the re-inclusion (penalty with status "active") to both, the failing and the non-failing parties.

On the following business day after the re-inclusion of the penalty, the CSD shall report the re-inclusion, either in the Daily Report (with the penalties computed for the previous day), or in the report of modified penalties:

- Amount of the cash penalty as it was when the penalty was removed;

- Status "Active"; and

- The standard reintroduction reason code (see Annex II).

## 8.3 RE-ALLOCATION OF AN EXISTING PENALTY

CSDs may re-allocate penalties, e.g. for a LMFP (Late Matching Fail Penalty), when the penalised party is not the real defaulting one (re-allocate from the instructing party to the delivering or receiving party, or from the delivering party to the receiving one).

The CSD shall re-calculate the amount of the penalty (because a different formula for calculating the penalty may apply, or due to changes in the reference data).

On the following business day after the re-allocation of the penalty, the CSD shall provide a report, either the Daily Report (with the penalties computed for the previous day), or the report of modified penalties, including the following information:

- For the initially penalised party and its counterparty:

  - Status "Removed";

  - A reason code to reflect the re-allocation (see Annex II); and

  - Optional: a description (free text) of the reason for the re-allocation (provided by the CSD).

- For the 'newly' penalised party and its counterparty:

  - Status "Active";

- A reason code to reflect the re-allocation (see Annex II);

- Optional: a description (free text) of the reason for the re-allocation (provided by the CSD); and

- A reference of the original penalty that has been re-allocated.

## 8.4 UPDATE OF EXISTING PENALTIES

Upon changes of values of the attributes of the securities subject to penalties (e.g. the ISIN, the value of the financial instrument type or the liquidity), CSDs shall recalculate affected penalties (i.e. those that used the modified reference data in their calculation) and update the penalty in case their details have changed, for example if there is a new amount due/ entitled to receive.

CSDs shall recalculate and update a penalty after changes in the related reference data as from when the updated information is known and latest until (and including) the 12$^{th}$ business day of the following month. The related reference data triggering the re-calculation and possible update of a penalty are:

- Changes in the reference price of a given ISIN for a given business day that was used for the calculation of the penalty;

- Changes in the values of the securities subject to penalties that was used in the calculation of the penalty (i.e. for a given ISIN, the changes of the value of the financial instrument type or its liquidity);

- Changes in the values of the daily penalty rate that was used in the calculation of the penalty (either the securities penalty rate or the currency cash discount rate).

On the following day, after the recalculation of a penalty, CSDs shall provide either the Daily Report (with the penalties computed for the previous day), or the report of modified penalties, including:

- New updated amount and values; and

- Reason code "Updated".

# 9 Cross-CSD settlement fails

## 9.1 Background

*Disclaimer: The settlement fails scenarios listed in this chapter have been discussed with ESMA but are yet subject to a formal approval.*

The scenarios consider whether or not a CSD in the chain is actually subject to CSDR and also illustrate which CSD is responsible for the calculation, reporting and/ or collection/ redistribution of penalty amounts, including when CSDs settle via the T2S platform.

Generally, the scenarios apply an "actual place of settlement" concept, i.e. the CSD where matching and settlement is ultimately taking place (i.e. where settlement finality is reached) is responsible for calculating the penalties ("Calculating CSD") and report them to its underlying participants (that may as well be CSDs) for processing and forwarding the reporting to their underlying participants and triggering the actual collection and redistribution of the monthly penalty amounts[43].

Relying on the Calculating CSD avoids that CSDs are calculating penalties in parallel (which anyway is not always feasible as e.g. late matching information is only available to the settling CSD), possibly leading to deviating results (e.g. due to different reference prices) and reconciliation needs[44].

In essence, the CSDR penalties must be applied by all involved CSDs whenever the ultimate matching and settlement is taking place in a CSD that is subject to CSDR (and if the underlying instrument and transaction are actually subject to the penalties regime), and in compliance with the CSD´s Terms and Conditions that bind all participants of that CSD, including when they are themselves CSDs (in or outside CSDR reach), as it is the case for CSD-direct links.

The investor CSD(s) is/ are responsible for the full collection and timely payment of the penalty amounts to the Calculating CSD (see chapter 7.5).

In case of a purely intra-CSD (i.e. CSD-internal settlement), the actual penalties application depends on whether or not the CSD itself is subject to CSDR or to an equivalent legislation.

---

[43] Note for T2S external settlement, T2S will (until further notice) calculate in any case. It will be up to T2S CSD to remove these penalties and replace them by the ones reported by the Calculating CSD.
[44] This approach is the same as today for those markets where penalties already apply.

## 9.2 SCENARIO 1A
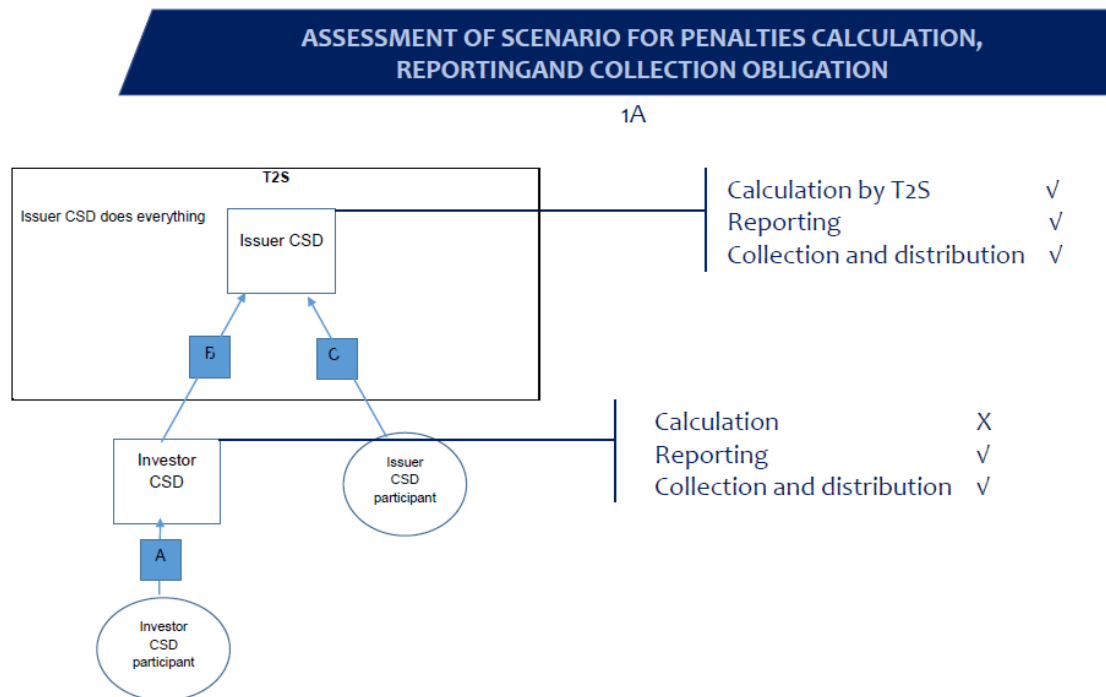


Due to its single settlement platform, T2S is able to calculate penalties for both legs of the T2S transaction.

## 9.3   SCENARIO 1B
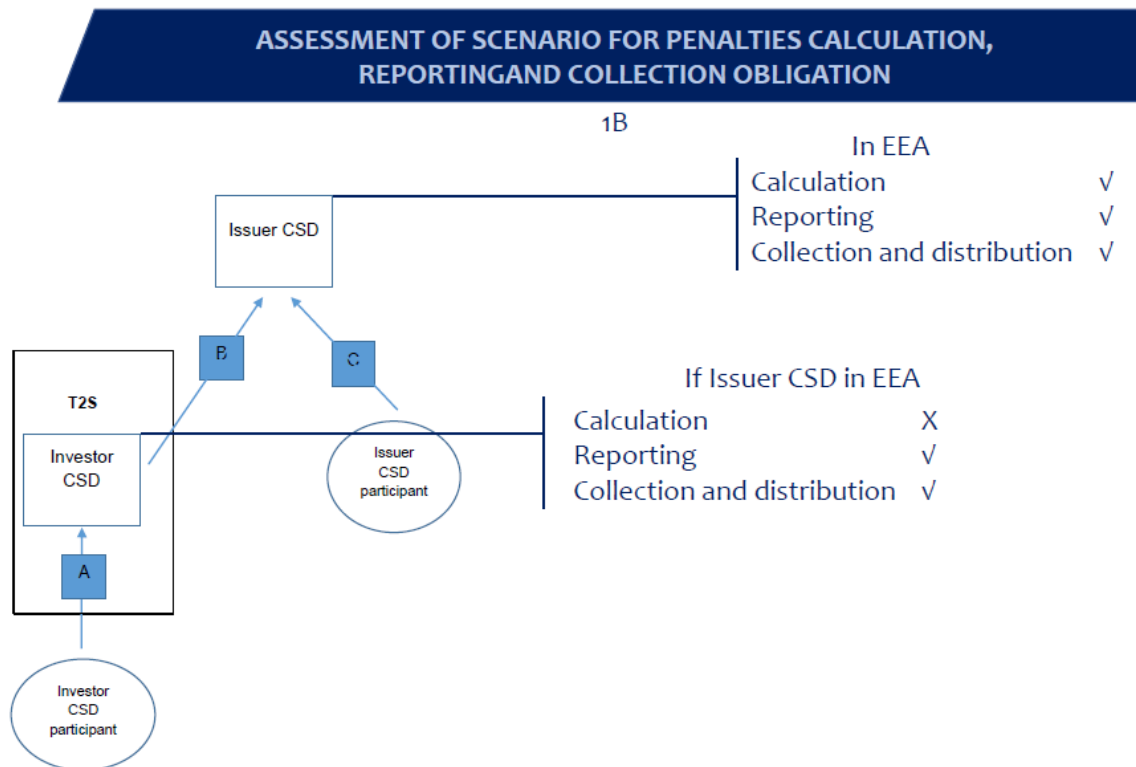


Only the Issuer-CSD has both legs of the transaction, allowing to calculate the ultimate penalties (however, due to T2S design, even for the single T2S leg, penalties will be calculated that may be overwritten by the Investor-CSD based on the Issuer-CSD reporting).

## 9.4 SCENARIO 1C



ASSESSMENT OF SCENARIO FOR PENALTIES CALCULATION, REPORTINGAND COLLECTION OBLIGATION

1C

T2S will calculate both as an investor and issuer CSD

Calculation on T2S   √
Reporting   √
Collection and distribution   √

Calculation   √
Reporting   √
Collection and distribution   √

Due to its single settlement platform, T2S is able to calculate penalties for both legs of the T2S transaction.

## 9.5 SCENARIO 2A



ASSESSMENT OF SCENARIO FOR PENALTIES CALCULATION, REPORTINGAND COLLECTION OBLIGATION

2A

T2S will calculate both as an investor and issuer CSD

Calculation √
Reporting √
Collection & distribution √

Calculation   X
Reporting   √
Collection & distribution   √

Calculation   √
Reporting   √
Collection and distribution   √

Due to its single settlement platform, T2S is able to calculate penalties for both legs of the T2S transaction.

## 9.6 SCENARIO 2B
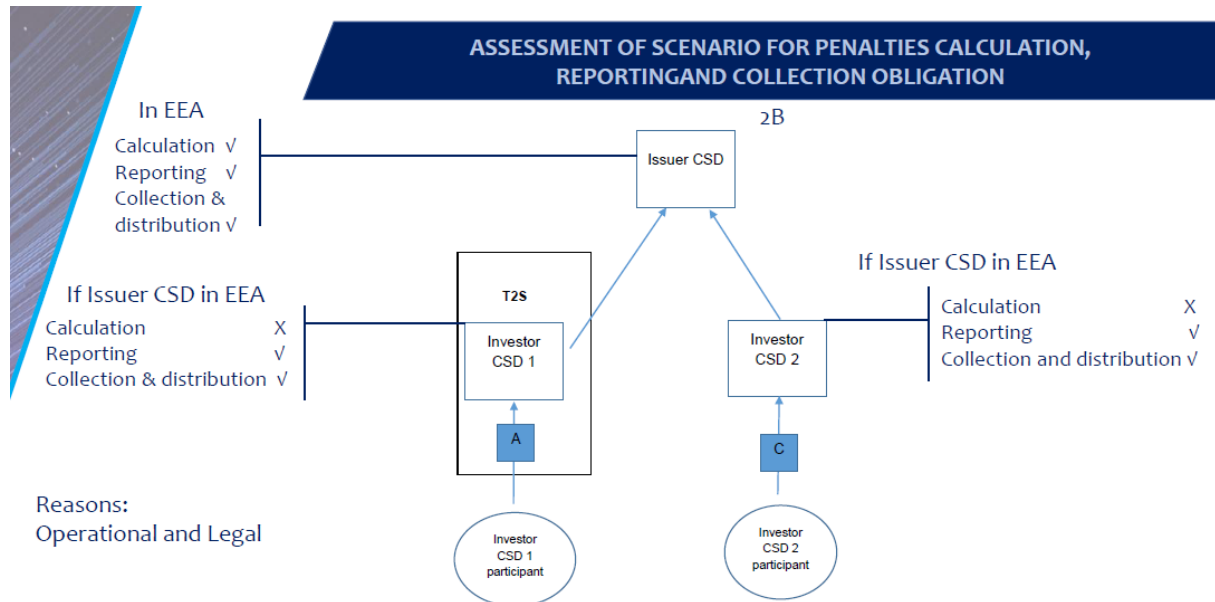


Only the Issuer-CSD has both legs of the transaction, allowing to calculate the ultimate penalties (however, due to T2S design, even for the single T2S leg, penalties will be calculated that may be overwritten by the Investor-CSD based on the Issuer-CSD reporting).

## 9.7 SCENARIO 2C
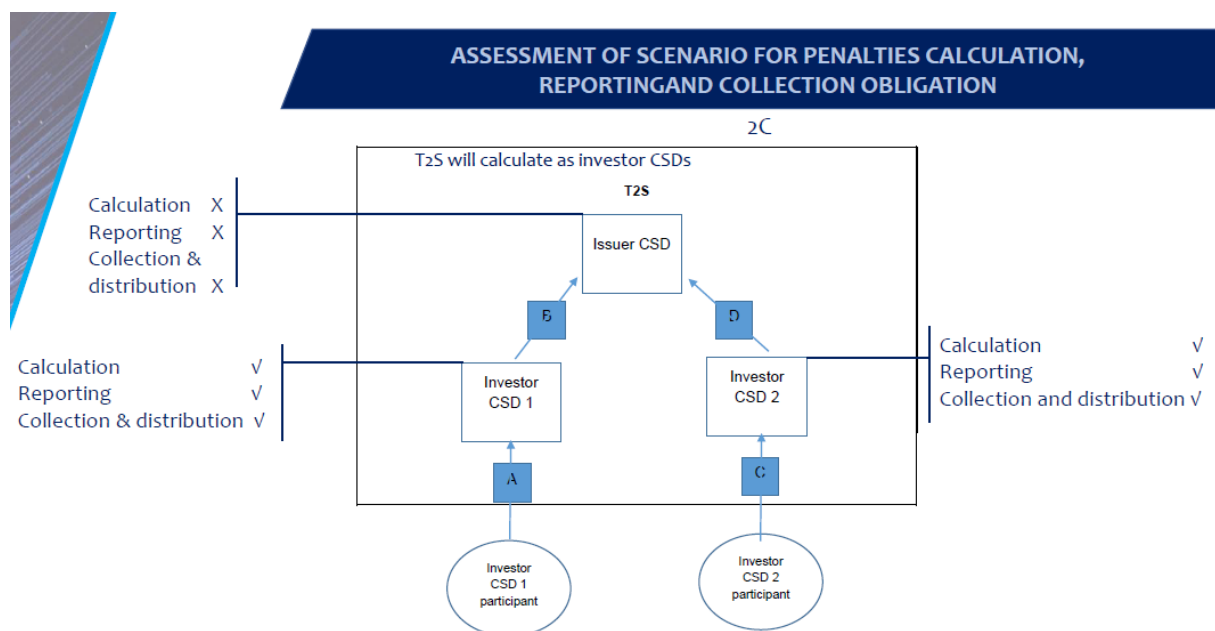
Due to its single settlement platform, T2S is able to calculate penalties for both legs of the T2S transaction.

## 9.8 SCENARIO 2D
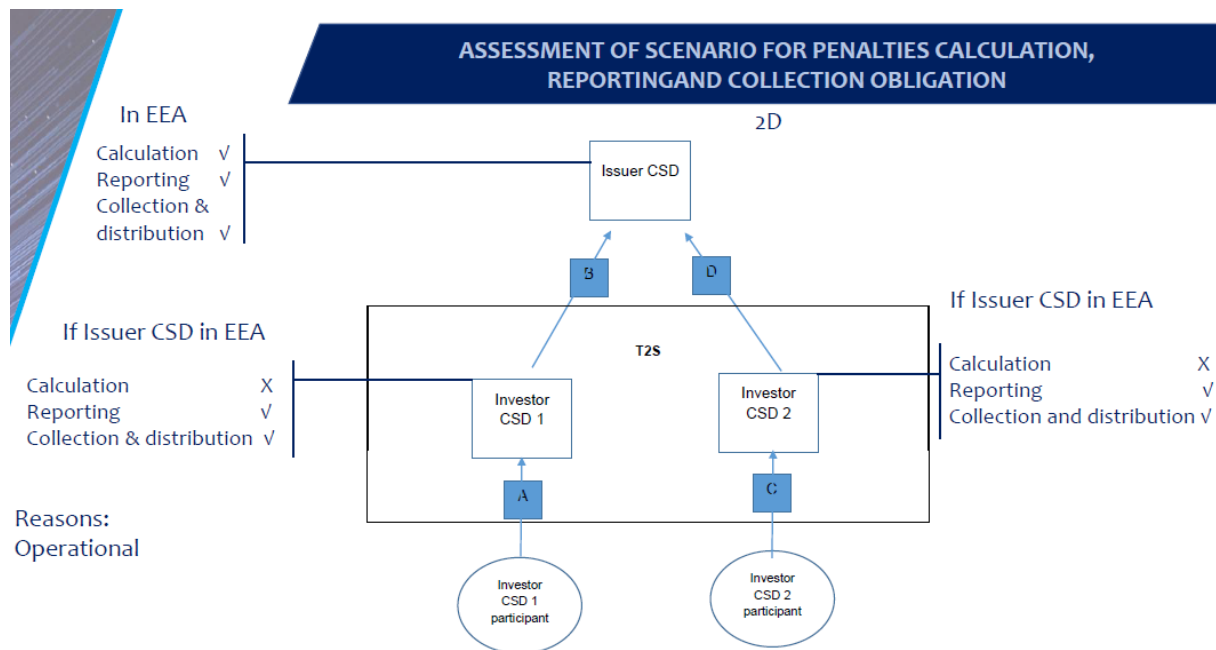


Only the Issuer-CSD has both legs of the transaction, allowing to calculate the ultimate penalties (however, due to T2S design, even for the T2S legs, penalties will be calculated that may be overwritten by the Investor-CSDs based on the Issuer-CSD reporting).

## 9.9 SCENARIO 2E
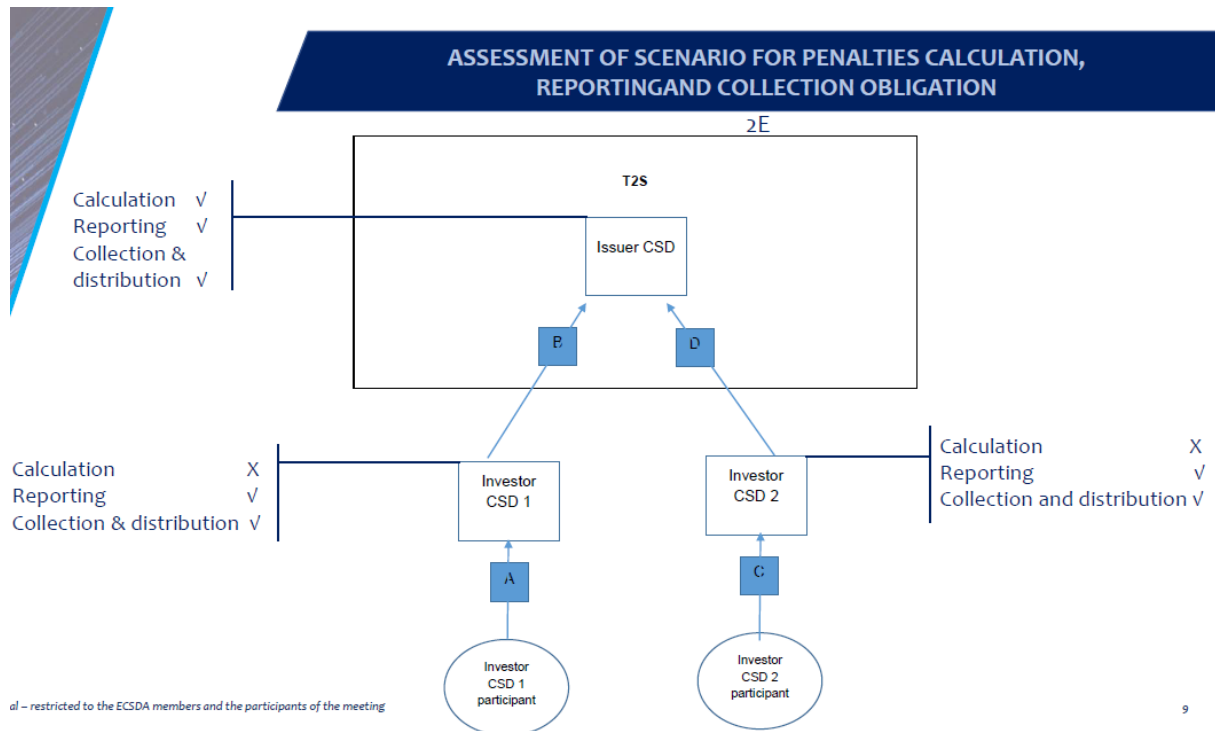


Due to its single settlement platform, T2S is able to calculate penalties for both legs of the T2S transaction.

## 9.10 SCENARIO 2F
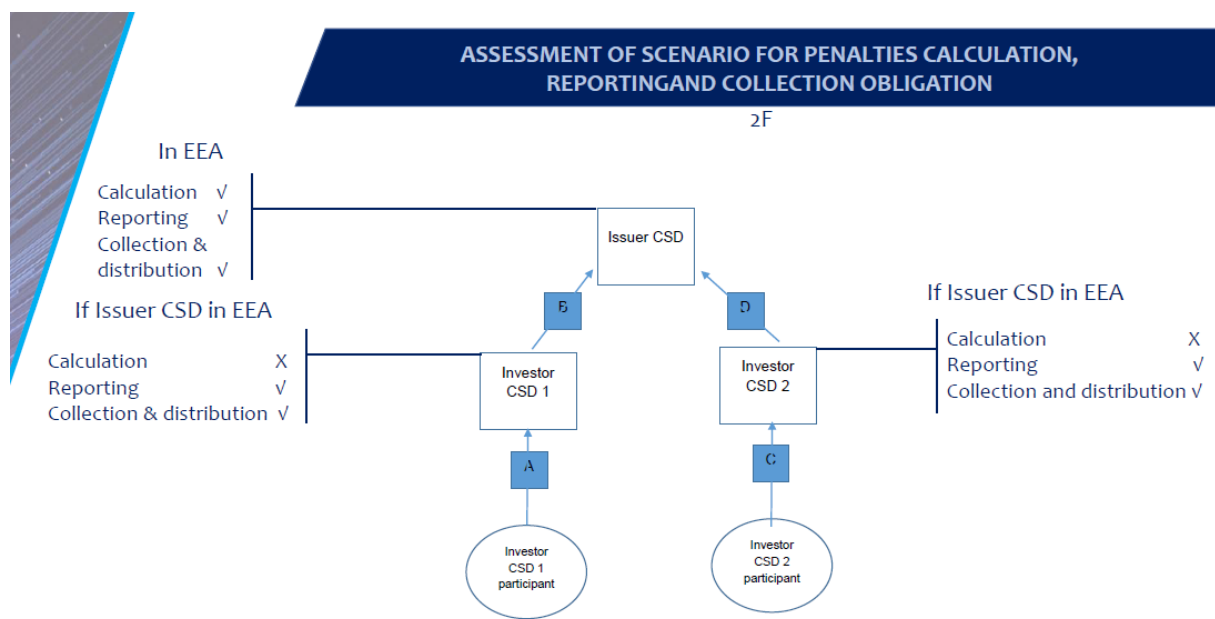


Only the Issuer-CSD has both legs of the transaction, allowing to calculate the ultimate penalties.

## 9.11 SCENARIO BRIDGE



Issuer CSD not subject to CSDR– case 20: ICSDs are investor CSD
Settlement between Euroclear Bank and Clearstream Banking Luxembourg
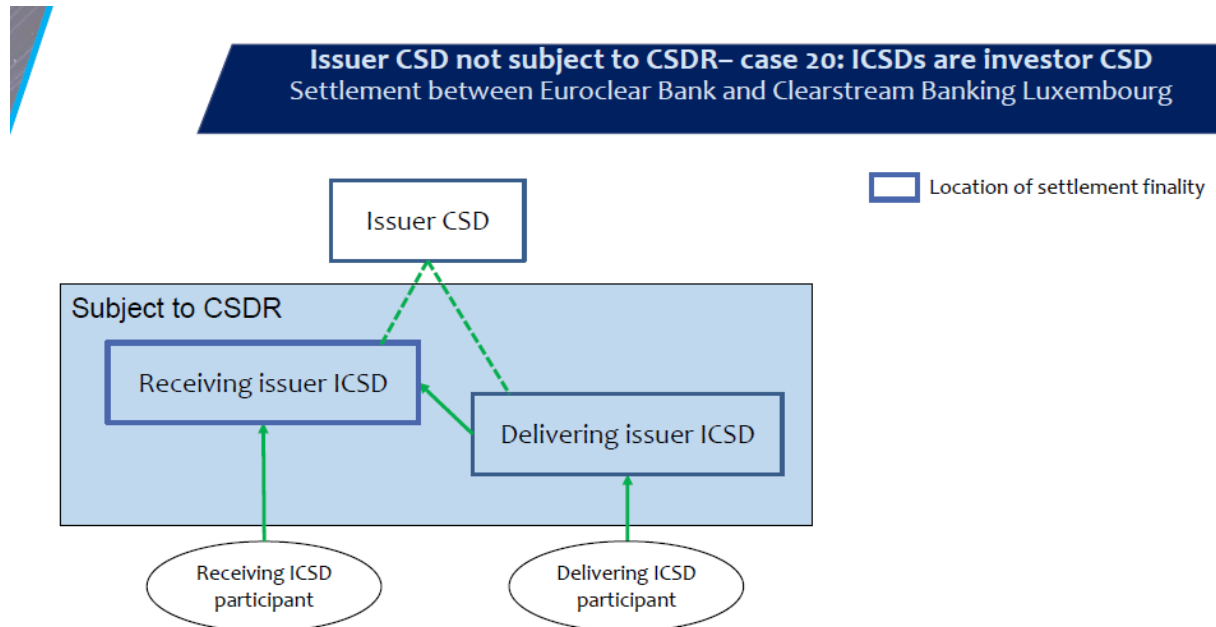
- Settlement taking place between both ICSDs, no movement in issuer CSD
- One ICSD to calculate penalties
- Both ICSDs to report penalties to their participants and regulators
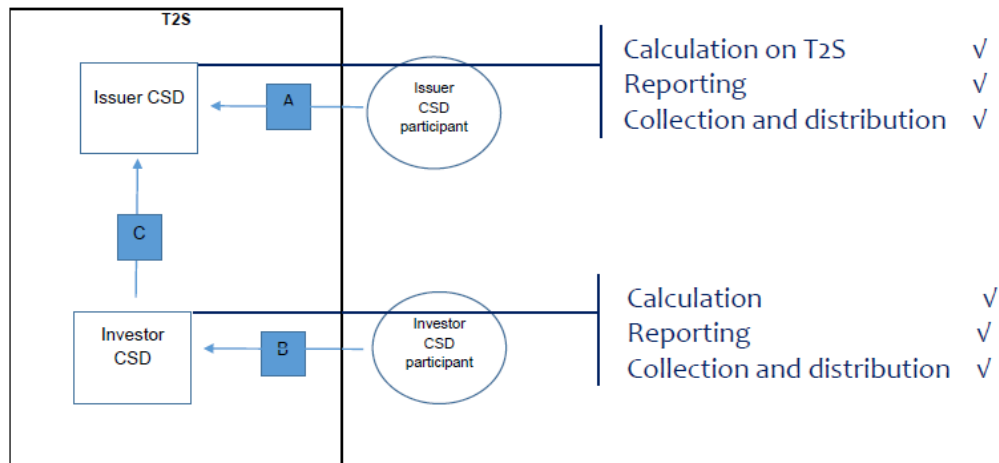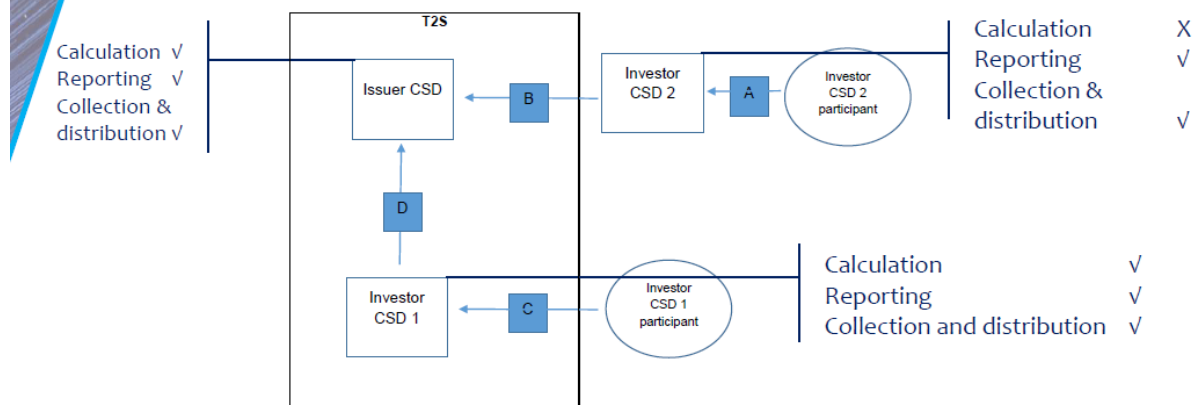- Both ICSDs to collect/distribute penalties from/to their participants

23

Note that the ICSDs´ realignment transactions on Issuer-CSD level are separately handled outside the Bridge settlement flow.

## 9.12 RECONCILIATION ASPECTS

Cross-CSD reconciliation differences are likely to occur at least in the following situations:

1. *CSD participant insolvency* (ESMA guidance pending)

CSDs should exchange information in case a CSD participant becomes insolvent, leading to the inability of the CSDs to (fully) collect the penalties due and potentially requesting the Calculating CSD to put (past, future or all) penalties to zero.

[OPEN POINT ESMA] The process will be detailed at a later stage when ESMA guidance has been issued until when penalties shall be calculated, reported or collected (and distributed) in relation to the insolvent participant ( e.g. CSD monthly reports to show the amounts as calculated but that will actually not be collected (or distributed) or put the penalty amounts to "zero" ?).

As a side note, it should also be considered that cash accounts closures (for reasons other than insolvency, on the level or a cash correspondent, central bank or other payment service provider)

may occur independent from the settlement/ penalties process. Hence, CSD participants shall ensure the penalties payments are made on time even in such situations.

2. *Suspension of settlement*

CSDR SDR RTS stipulate that no penalties shall be applied once a CSD has suspended settlement of an ISIN, e.g. due to an "undue creation/ deletion of securities" reconciliation break.

Similar to insolvency handling, CSDs must exchange information in case e.g. an Investor-CSD suspends an ISIN from settlement leading to the inability of the Calculating (Issuer-)CSD to (fully) collect the penalties due in case only the Investor-CSD applies such suspension (i.e. the suspending Investor-CSD would cease penalties application while the Calculating (Issuer)-CSD continues to calculate them).

As a CSD must not distribute penalties it has not collected, settlement suspension may require consideration in the reconciliation and monthly payment process.

The process will be detailed at a later stage.

# 10 COLLECTION & REDISTRIBUTION OF PENALTIES (PAYMENT)

**OPEN ITEM ECSDA: This chapter is to be considered as "work in progress" subject for continuing discussions within ECSDA in various aspects, like cross-CSD cash exchanges, currency issues (see Chapter 6) and applicable payment processes (direct debit, PFOD etc.).**

## 10.1 GENERAL OVERVIEW

Collection and Redistribution of Penalties refers to the monthly, actual exchange of cash-amounts (separate for every single currency in which penalties were calculated and reported) resulting from the calculation as described in chapter 7.5.

CSDs and CSD participants shall collect/ re-distribute the full amount of penalties that were reported to them within the timeline described in chapter 2.

CSDs use their own dedicated cash accounts for the purpose of this process; they shall not take any financial nor counterparty risks. In case parties fail to pay, the CSD itself will fail to (partially or in full) pay further to its participants expecting the cash.

Investor-CSDs that are already opposed to financial risk based on their role as a participant at the Calculating CSD may apply deviating procedures from what is described in this document.

WORKING ASSUMPTION ECSDA: Depending on their set-up (having/ not having a banking license) and national specificities, CSDs will use different models for the actual penalties payments processing.

The following possible payment models were identified:

1. CSD triggers direct debits[45] and/ or cash transfers;
2. CSD generates PFOD instructions (see footnote[46] for details);
3. Usage of a payment bank[47].

It shall be noted that:

---

[45] ESMA was asked to acknowledge the risks related to CSDs not being allowed to perform direct debits in some countries and to consider appropriate mechanisms to enforce the timely payment of due amounts.

[46] A common dummy ISIN code must yet be defined for application by all CSDs. PFOD trade date would be 15th BD, ISD 17th BD of the payment month. All (delivery and receipt) PFODs should be generated at the same time, "already matched" (unless for cross-CSD penalties payments), they should contain a 'non modifiable' and 'no partial' (NPAR) flag and contain highest possible settlement priority. In case second level matching information is required, the CSD BIC shall be used (if possible). Note that due to the application of a dummy ISIN code, in case such PFOD fails on its ISD, settlement penalties will **not** apply as the ISIN is not listed in the relevant FIRDS database.

[47] Option 3 appears to be least preferred by CSDs due to extended payment chains (via CCBs), increasing risk of delayed payments. However, for foreign currency transactions this may be the only feasible option.

- CSD participants need to provide their CSD with the cash-account details for each relevant currency on which they will manage their penalties (CSD participants will be free to decide on which cash account they want to manage their penalties, be it their default settlement cash account, or otherwise dedicated penalties account, as long as this complies with the CSD payment processing method).
- CSDs shall, when applicable share their penalty cash-account details with the relevant parties (CSDs, cash-correspondents, CSD participants or other).

CSDs may define appropriate measures (to be described in the relevant contractual documents with the CSD participants) to ensure penalty amounts due are available to the CSD and CSD participants comply with their payment obligations to the CSD on time to avoid delays and processing issues due to a lacking or incomplete penalties collection on the 17th business day.

ECSDA assumes that CSDs may (if allowed under applicable laws) disclose the name of a participant, imposing fines, etc. if a participant has not covered its penalties payment obligation fully or in time on single or re-occurring occasions.

The process of collection and redistribution has to be managed in a phased approach to make sure CSDs do not pre-finance any payment. The overall payment process consists of the following four main steps:

1. Collection from participants which are not investor-CSDs
2. Redistribution from investor-CSDs to Calculating CSD
3. Redistribution from Calculating CSD to its participants (incl. Investor-CSDs)
4. Redistribution from Investor-CSDs to its participants

Steps 2 and 4 apply only in case of penalties on cross-CSD settlement fails.

These steps shall be performed completely on the same day for every currency involved.

Cross-CSD aspects:

OPEN ITEM ESMA: ESMA to endorse that the re-distribution steps may be done in priority to payments between CSDs, i.e. CSDs will start the re-distribution process by crediting first their participants which are CSDs.

It has to be noted that the Calculating CSD will treat an Investor-CSD the same way as any other CSD-participant. Differences exist in the collection process where direct debit on the Investor-CSD cash account or creating a PFOD instruction in released mode on behalf of the Investor-CSD is not allowed.

It is at the discretion of each CSD to decide whether it starts the redistribution process (partially) only once the collection process has been completed fully or not. The decision will mainly depend

on the possibility of the CSD to hold overnight cash-position and depends on capabilities, banking-licences and approvals from regulators[48]:

- CSDs not allowing overnight position need to pay out the money they received the same day.
- CSDs allowing overnight position will usually wait for the collection process to be fully completed to avoid above scenario. In case of participants not paying in time, the CSD keeps a balance overnight. The CSD will have to inform its participants of the delay.
- Alternatively, with regard to collection and to avoid overnight balance, CSDs could make cash reservations during the payment day. If not all collections are fulfilled, reservations can be released by EOD and re-start the process on the next day again.

CSDs shall not issue "invoices" for the payments relating to the transfer of penalties. After the calculation is done (see Chapter 7) and the monthly aggregated report was sent (see Chapter 11), the transfer of the cash relating to the penalties shall take place.

CSD costs for its penalty mechanism may be charged to its CSD participants but have to be separated from the settlement fails penalties application and payments process[49].

## 10.2 STEP 1: PENALTIES COLLECTION FROM PARTICIPANTS WHICH ARE NOT INVESTOR-CSDS

Participants (that are not themselves CSDs) must pay their dues to the CSD, on a dedicated CSD cash account for the management of the penalties, latest on the 17th business day by 09:00 a.m. CET but latest 2 hours prior the cut-off time of the relevant currency payment system; see as well chapter 2 for details).

An investor-CSD must make sure, that it collects the cash onto the accounts (per currency) for payment to the Calculating CSD. In case an Investor-CSD has accounts with several Calculating CSDs, these may be different accounts.

---

[48] Note from ECB: impacted CSDs could check with their regulators if they could consider the settlement of penalties stemming from CSDR as being intrinsically a CSD activity and not a banking one and hence it would not be necessary to have a banking licence for carrying out these transactions (e.g. in T2S, some CSDs without banking licence are for instance using PM accounts today for settling coupons).

[49] Invoices shall only be used by the CSD to recharge its development and running costs relating to the management of its penalty mechanism (see extract from the CSDR SDR RTS - Article 18 (3): *"CSDs shall charge participants separately for the costs of the penalty mechanism (...)"*). Content and design of the invoices depend on the cost distribution approach applied by the CSD and cannot be harmonized.

To not delay the cash collection and redistribution process, no tolerance between the amount to be paid and the amount actually collected is allowed, i.e. CSD participants must pay <u>exactly</u> the amount as calculated and reported by the CSD.

Unless PFOD instructions are generated by the CSD, payment pre-advices per currency shall be issued by each CSD that represent the actual amount to be paid by a CSD participant.

Should the amount received by a CSD not represent the one expected, the CSD may not be able to perform the penalties re-distribution to its participants (including other CSDs in a cross-CSD penalties scenario)[50].The collection process might be performed via several methods, depending on the CSD profile (with or without a banking license), and the CSD local specificities. The model to be used will be at the discretion of the CSD, which will have to inform its participants accordingly.

Excluded from the collection process, unless otherwise agreed between the two CSDs, are payments that have to be done by an Investor-CSD to the Calculating CSD. This process step is called 'Redistribution from Investor-CSD to Calculating CSD' and described later.

There are different mechanisms available to the CSDs on how to collect the penalties:

### 10.2.1 Payment via direct debits and/ or cash transfers

#### 10.2.1.1 Direct debit
Whenever legally and/or contractually allowed, the CSD shall collect the money by directly debiting the cash accounts of its participants (that are not themselves CSDs). Such process will avoid delays and differences in the amounts expected and collected by the CSD and subsequent blocking of the cash distribution process.

CSD participants must have adequately funded their penalties cash account on time. In case the participant penalties cash account is not sufficiently funded, the direct debit may lead to in an account overdraft.

#### 10.2.1.2 Cash transfer (no direct debit applied)

In the case when direct debit is not feasible, the CSD participants will have to actively transfer the amounts due to the dedicated cash account of their CSD. The CSD participants shall credit the amounts due to the CSD´s dedicated cash account latest by 10.00 a.m. CET on the 17th business day of the month.

### 10.2.2 Payment via Payment Free of Delivery (PFOD) settlement instructions
<mark>OPEN ITEM (ECSDA DISCUSSION ONGOING)</mark>

Ahead of the 17th business day, the CSD will create PFOD instructions to receive the cash amounts from its participants that have to pay penalties. These intra-CSD PFOD instructions may be sent as already matched instructions (if this functionality does exist in the CSD)[51]. The PFOD settlement

---

[50] Note that some CSDs may today not be allowed to keep cash balances overnight. For the purpose of cash penalties processing, impacted CSDs shall arrange for an exception agreement with its relevant NCA.
[51] Usage of the already matched feature is possible in an intra-CSD context, as the CSD has the rights on all its participants accounts.

will lead to a credit of the CSD penalties cash account and a debit of the CSD participant´ penalties cash account.

CSD participants must have adequately funded their penalties cash account, in order for the PFOD to timely settle on the 17th business day.

Note: With the use of the PFOD instructions, the rules of the Settlement platform will be the ones to be applied (i.e. recycling, reporting … ).

### 10.2.3    Payment via a payment bank

In some cases, the penalties payment process may involve a third party acting as a payment bank. Such payment bank will have to follow one of the two methods above mentioned.

## 10.3  STEP 2: PENALTIES REDISTRIBUTION FROM INVESTOR-CSD TO CALCULATING-CSD

While a delay in the cash redistribution process is considered less relevant in a purely intra-CSD relation, it will have ripple effects when penalties are to be exchanged across CSDs.

The Calculating CSD is not allowed to directly debit the Investor-CSD.

Therefore, only the below mechanism will be available for payments from an Investor-CSD to the Calculating CSD.

### 10.3.1    Cash transfer (no direct debit)

The Investor-CSD has to pay to the dedicated cash account of the Calculating CSD.

Usually via its Cash Correspondent Bank, either the CSD that owes the penalties amount will send a wire transfer to the CSD to be credited, or the CSD to be credited will send a cash transfer to debit the CSD that owes it a penalties cash amount.

In case the CSD penalties cash account is not sufficiently funded, the debit transfer shall be recycled until cash is available. The cash transfers have to be done latest on the 17th business day.

### 10.3.2    Payment via PFOD transactions

Ahead of the 17th business day, the CSD will create cross-CSD PFOD instructions[52] to:

- receive the penalties cash amounts from its participants that are themselves CSDs; or
- pay the penalties cash amounts to its participants that are themselves CSDs.

Each CSD instructs its leg of a PFOD transaction and matches it at the Calculating CSD. The investor CSD can use hold/ release functionality to control the payment.

---

[52] In a cross-CSD context, the use of the already matched feature is not possible, as the CSD does not have the rights on other CSDs.

In case the Investor-CSD is not allowed to hold overnight cash position, partial payment to the Calculating CSD may be performed if it supports partial-(PFOD) settlement.

An agreement is needed amongst involved CSDs in order for the matching to take place.

Note: with the use of the PFOD instructions, the rules of the settlement platform will be the ones to be applied (i.e. recycling, reporting or other relevant rules).

### 10.3.3   Payment via a payment bank

CSDs may outsource the penalties payment process to a third party acting as a payment bank. Such payment bank will have to follow one of the two methods above mentioned.

## 10.4  STEP 3: PENALTIES REDISTRIBUTION FROM CALCULATING-CSD TO PARTICIPANTS (INCL. INVESTOR-CSDS)

As soon as a CSD re-distributed the cash amounts due to the other CSDs (if applicable), it shall fulfil its obligations towards its other participants that are not CSDs and initiate the payments to re-distribute the cash due to its participants.

This is the last step for the Calculating CSD and will clean its dedicated cash-account. Payments to Investor-CSDs must be given highest priority to avoid ripple effects in cross-CSD settlement fails penalties payments scenarios.

Two mechanisms are available for payments from Calculating CSD to participants including Investor-CSDs:

### 10.4.1   To use cash transfers

The CSD might transfer the amounts due to the dedicated cash account of their participants. Such credit shall take place once the payments due have been (fully or partially, as the CSD may decide) collected on the 17th business day.

### 10.4.2   Payments via Payment Free of Delivery (PFOD) settlement instructions

Ahead of the 17th business day, the CSD will create PFOD instructions to deliver the cash amounts to its participants that have to receive penalties amounts.

These intra-CSD PFOD instructions may be sent as already matched instructions (if this functionality does exist in the CSD)[53].. These PFODs will debit the CSD penalties cash account and credit the CSD participants´ penalties cash accounts.

Note: With the use of the PFOD instructions, the rules of the Settlement platform will be the ones to be applied (i.e. recycling, reporting or other relevant rules).

---

[53] Usage of the already matched feature is possible in an intra-CSD context, as the CSD has the rights on all its participants´ accounts.

### 10.4.3 To outsource the management to a payment bank

CSDs outsource the penalties payment process to a third party acting as a payment bank. Such payment bank will have to follow one of the two methods above mentioned.

## 10.5 STEP 4: PENALTY REDISTRIBUTION FROM INVESTOR-CSDS TO PARTICIPANTS

Processes are identical to step 3.

## 10.6 EXCEPTION HANDLING: PARTIAL PAYMENT TO CSD PARTICIPANTS

WORKING ASSUMPTION: In principle, to ensure equal treatment of participants and to avoid that CSDs take risks resulting from the management of the settlement fail penalties mechanism incompatible with CSDR, CSDs should only start distributing penalties when the amounts due are collected in full.

However, while the exact global amount, as reported by the CSD, has to be the one paid by the CSD participants (and no partial payments should be done), some issues might occur:

In case only parts of penalties amounts have been collected by the CSD, the re-distribution process might or might not be triggered. This will be at the discretion of the CSD, which will have to inform its participants accordingly:

- Assuming not all participants pay their obligation in time, the CSD cannot satisfy all of its participants (some might receive only part of it or even nothing).
- Some CSDs may consider re-distributing the penalties amounts as soon as they have received them. This re-distribution process will be made randomly (without checking which participant indeed paid or not).

Other CSDs may consider waiting for the full collection of the penalties amounts to be done, prior starting the re-distribution process. Impacts in case of cross-CSD scenarios are yet to be analysed.

Partial payments may be performed by the payment processing means as described in the previous chapters.

In case of PFOD payments, ideally, PFOD partial settlement could be applied (if available).

Illustrative example:
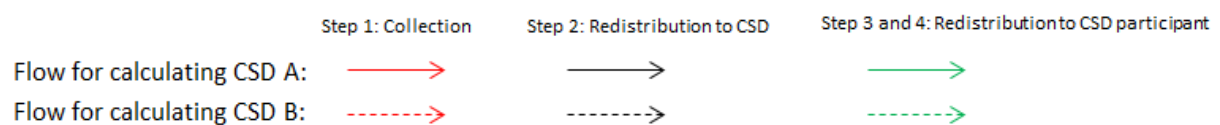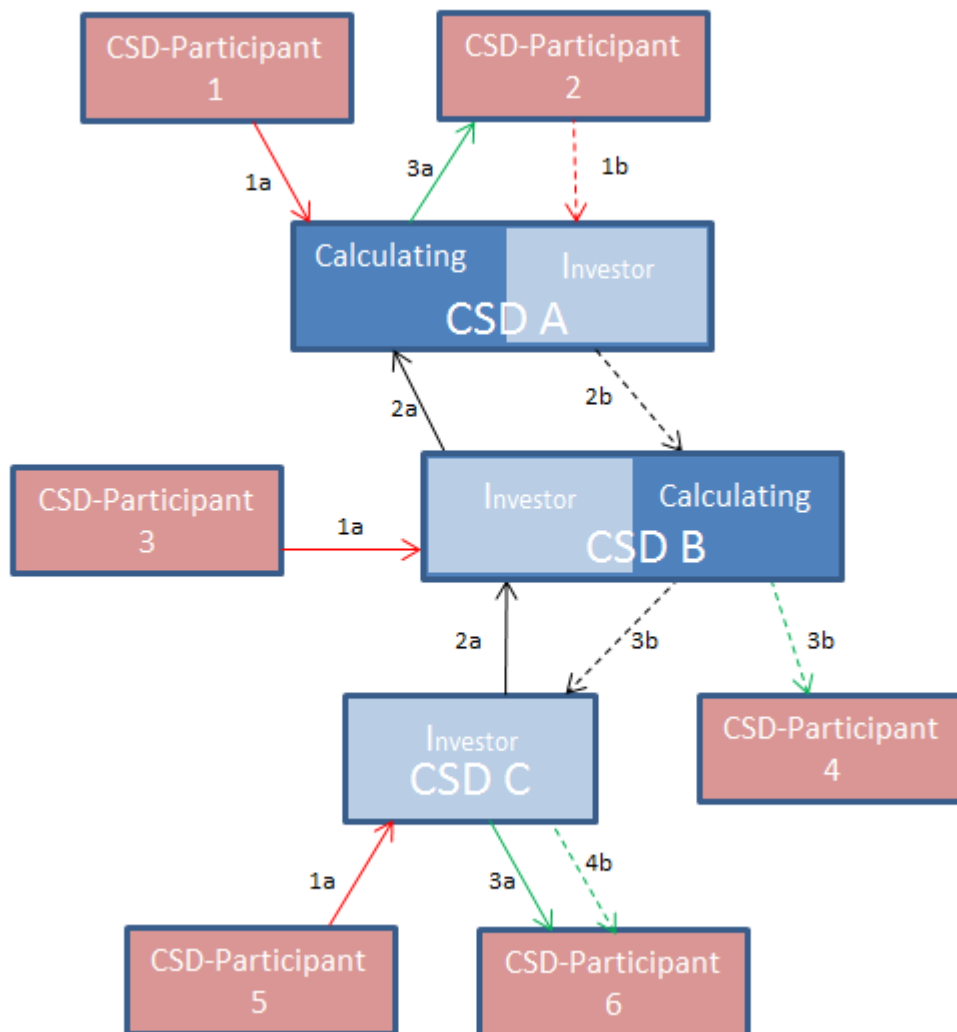


Description:

- CSD A is Calculating CSD and has three participants whereas one of them is an Investor-CSD. CSD A is also Investor-CSD at CSD B.
- CSD B is Calculating CSD and has four participants whereas two of them are Investor-CSDs. CSD B is also Investor-CSD at CSD A
- CSD C has two participants and is Investor-CSD at CSD B. CSD C uses CSD B as an agent for settlements at CSD A.

Cash-flow description:

The continuous lines reflect the collection & redistribution flow for settlements at CSD A

1a --> Step 1: collection of penalties. Full amount.

2a --> Step 2: redistribution from investor CSDs to Calculating-CSD. Full or partial amount.

3a --> Step 3: redistribution from Calculating-CSD to participants. Full or partial amount.

No step 4

The dashed lines in the illustration above reflect the collection & redistribution flow for settlements at CSD B

1b --> Step 1: collection of penalties. Full amount.

2b --> Step 2: redistribution from investor CSD to Calculating-CSD. Full or partial amount.

3b --> Step 3: redistribution from calculating CSD to participants and Investor-CSD. Full or partial amount.

4b --> Step 4: redistribution from Investor-CSD to participant. Full or partial amount.

# 11 REPORTING

For the purpose of exchanging penalties related information between CSDs and their participants (including those that are CSDs) in a Straight Through Processing fashion, penalties reports content and formats used by CSDs shall be harmonised. Such approach will enable all involved parties to apply a common messaging and communication process, by using ISO reports for Application-to-Application (A2A) message exchanges.

This is especially relevant in the context of cross-CSD settlement and customers being participants of multiple CSDs.

Proprietary solutions to report penalties may be used by CSDs as additional (User-to-Application; U2A) communication means[54], for example to support participants demand or address market specific aspects.

This Framework chapter focuses on providing a high-level overview of the information to be provided in the respective messages and reports.

However, the final specifications will be agreed with and made available by the standards setting organisations.

## 11.1 REPORTING FORMATS

T2S/ 4CB has drafted dedicated daily and monthly penalties ISO 20022 reports. Once developed, the relevant ISO 20022 message could also be available to non-T2S CSDs.

The existing ISO 15022 messages MT537 and MT548[55] will be adapted by SWIFT to cover penalties related information. Note that the MT548 will only be usable for the reporting of daily penalties (but not the monthly aggregated reporting).

CSDs should use the ISO 20022 and /or ISO 15022 messages, when they are available.

This section describes penalty reports, as well as subsequent cash payment-related messages.

All reports exchanged between CSDs and provided from CSDs to their participants shall be identical in terms of the applied formats.

### 11.1.1 ISO 20022 messages

For the ISO 20022 format, it is proposed to use a Pillar III semt.044[56] message dedicated to penalty messaging. The features of this message are as follows:

---

[54] For the exceptional cases where a CSD may use other standards, please refer to the ESMA Questions and Answers to the CSDR on article 35, CSD Question 4 (a) under the Conduct of business rules. The document can be found here: https://www.esma.europa.eu/press-news/esma-news/esma-updates-csdr-qas-0

[55] The adapted MT message will be made available in November 2019. Please refer to the SMPG, Standards MT Release November 2019, Settlement and Reconciliation.

[56] The exact nomenclature for the semt.044 message draft is under SWIFT creation.

- It is a message dedicated to penalty reporting and its peculiarities (new information fields);

- It uses the most recent ISO standard in XML format;

- It is to be used as primary message for penalties reporting;

- It will have hierarchical blocks, repetitive for every party. These repetitive party blocks will contain repetitive blocks for counterparties, with the specific penalties information (report->party->counterparty->penalty). These repetitive blocks might ease the processing of reports further down the line as they will already contain the needed block of information; and

- The proposed message contains fields going beyond the potential group of mandatory fields and can possibly accommodate also optional and additional fields if needed.

The penalties amounts will contain a "credit" (for amounts to be received by the CSD participant) or "debit" (for amounts to be paid by the CSD participant) indicator.

In regard to ISO 20022 formatting, it is possible to have reports also in the form of proprietary solutions (see 11.1.3) for U2A information exchanges.

### 11.1.2 ISO 15022 messages

#### 11.1.2.1 *Penalties calculation reporting:*

MT537, 548 SWIFT ISO 15022 messages will be adapted to cover as well penalties information transmission (new "PENA" block)[57].

The following development of the standard was agreed by SMPG:

MT537 (Statement of transactions) and MT548 (Securities Settlement Status Advice) adaptations to contain a dedicated new sequence specific to the penalties reporting, in order to avoid any rejection of a 'standard' MT537 or MT548 received after the settlement of the transaction.

It means that MT537/ 548 "PENA" are expected to include new fields and repetitive blocks (such as late matching/ settlement fail; reporting of underlying transaction; penalty ID; credit/debit indicators; calculation parameter references). It is expected that the new fields would correspond to the new ISO 20222 message in their content and level, although there might be alternative approaches to the content of some fields, if the nature of the field requires it.

The penalties amounts will contain a "N" indicator for amounts to be paid by the CSD participant.

#### 11.1.2.2 *Penalties collection and redistribution (payments) reporting:*

CSDs shall inform their participants of the actual amounts (debit or credit) of the penalties, via a dedicated reporting used as a payment pre-advice. It could be done either viaCash messages or Settlement messages (managed by each CSD under the format it deems appropriate.

---

[57] The following Change Requests relevant to the CSDR Settlement Discipline are expected to the implemented through the November 2019 SWIFT release: CR 001449, CR 001446, CR 001463, CR 001447.

For further details, see chapter11.3.3.

Payment pre-advices for amounts to be paid shall be issued on the 15<sup>th</sup> business day; no payment confirmations are required to be issued once the payment has been executed.

### 11.1.3    Alternative reporting solutions

In addition to the above-mentioned messages, in regard to the exchange of reports, CSDs may develop User to Application (U2A) interfaces for or alternative forms of delivery of reports for the benefit of their participants.

For U2A, formats other than XML (i.e. csv, xls, xlsx) might be used.

Baseline reporting solutions are however ISO 15022 and IS O20022 messages, which are, therefore, the minimum and mandatory reporting to be offered by all CSDs to their participants.

## 11.2   GENERIC REPORTING CONTENT

### 11.2.1    Information blocks for penalty reporting

The corresponding SWIFT ISO messages described in chapter 11.1 refer to the content of relevant information fields.

However, in order to harmonise the interpretation of the relevant fields on a pan-European level, the intended hierarchy and content of those fields are described below.

The penalty reports will have a hierarchical structure wherein the level within the hierarchy will indicate:

- the level of aggregation;
- the reporting element.

These levels will, in technical terms, correspond to repetitive blocks within the reports, regardless of which ISO format is used.

This way, the high-level report will consist of repetitive blocks, each one representing an individual reporting segment/ level:

**T - Technical level**

This type of data is of a technical nature stating the specifics of a report. This sort of information- being metadata and being, therefore, mandatory for every produced report- falls not strictly within the hierarchical division of provided information.

**A - Report issuer level (**If the non T2S CSD itself manages the calculation process, then this level becomes obsolete)

This level of information provided refers to high-level reports or master reports which are available to CSDs (either produced by themselves or by third parties as in the case of the T2s Penalty Mechanism).

**B - Participant level**

This level of reporting states information relating to a specific participant (be it a regular participant, CCP, Investor CSD or other).

**C - Counterparty/ Penalty level**

At this level, a specific participant will be informed within the positions against specific counterparties about the actual penalties. This applies for Daily reports, as well as Monthly reports, with the needed details at penalty and transaction level.

### 11.2.2   Mandatory fields

Mandatory fields ensure that the recipient of a penalty report will always be able to identify a penalty, i.e. even though he would have to use information from his internal sources.

For example, a penalty report recipient would be informed about the amount of a penalty. In order to identify it, he would need to know:

- the instruction/ transaction ID;
- the day for which the penalty was computed.

In order to understand the penalty, the recipient would need[58]:

- the Security penalty rate and/ or the penalty discount rate for the currency;
- the SME Growth Market indicator (only for those settlement fails where the transaction was actually concluded on a SME Growth Market trading venue);
- the Liquidity indicator; and
- the amount to which the penalty applies (in case of partial settlements).

However, it will have to be made sure that in a cross-CSD context, the receiving CSD will always be able to allocate the penalty correctly to its underlying participants.

Mandatory fields have to comply with the mapping standards of the penalty reporting.

Penalties and penalty aggregates in penalty reports will be always reported in the currency, in which the penalty amounts were calculated, i.e. no conversion will take place except the possible conversion during the calculation process (see chapter 6 and 7.4).

**DRAFT - XML fields  (yet to be checked for T2S terms and alignment with chapter 9 settlement scenarios)**

| Group of variable identifier | Name of T2S benchmark identifier | Informational content of the identifier |
|---|---|---|
| Instruction IDs | Account Owner Transaction Identification | The ID of the instruction on holder level |

---

[58] Note that the "reference price" used by the CSD for the penalty calculation for the failing instrument will not be displayed; the respective message field, if part of the report, may be blank or contain NONREF or similar information.

| | | |
|---|---|---|
| | Account Servicer Transaction Identification | The ID of the instruction on custodian/intermediary level |
| Transaction IDs | Processor Transaction Identification | The ID of the transaction on the level of the sending SSS |
| | Market Infrastructure Transaction Identification | The ID of the transaction on the level of the master SSS |
| | Common Identification | The ID as referenced to both side of the transaction on master SSS level |
| | Related Transaction Identification | Master SSS´ reference of sending SSS´ transaction ID |
| | | |
| Security account number and party identification | Safekeeping Account | Accounts can be layered and there shall be assurances that when a CSD states in the penalty report a specific Security account number (and possibly the account owner), that it will be correctly understood by the other CSD (as they might have their own unique account structure). |

## 11.3 MESSAGE TYPES

There are several types of reporting on penalties throughout the month (see chapter 2):

1. Daily reporting of penalties;

2. Monthly aggregated reporting of the penalties over the period;

3. Payment pre-advices (either via Cash or Settlement messages) which inform about actual payment amounts to be received or paid (.

### 11.3.1 Daily Penalties report

Penalties are computed for and reported to the relevant **failing and non-failing party**. The CSD will hence report twice each penalty computed:

1. To the failing party (i.e. party imposed with the penalty), and

2. To the non-failing party (i.e. party entitled to receive the penalty).

The **failing party** (party imposed with the penalty) and the **non-failing party** (party entitled to receive the penalty) are the two counterparts responsible for the settlement of the underlying transaction and consequently the respective **owner of the securities account**.

It shall be noted that, in case of a "cross-CSD scenario" (see chapter 9), the CSD will consider the other involved CSD as the owner of the relevant securities account of the underlying settlement instruction.

Within the messages:

- The party shall be a repetitive block in order to be able to include all the information in a single message. The CSD shall report cash penalties for a given party sorted by CSD (for cross-CSD fails), currency and counterparty of the penalty (i.e. non-failing or failing party, respectively).

- Each penalty computed for a given business day and reported to the failing/ non-failing party and/ or its CSD shall include the details listed in chapter 11.2.

- It is understood that an individual penalty contained in the report of a specific participant will have a mirror entry (debit vs. credit) in the penalty report of the relevant counterparty, i.e. will be on the participant level reported in two penalty reports.

- The daily reports contain only the amounts and information for a specific business day, i.e. they do not reflect exposures accrued in the course of several fail days[59].

### 11.3.2    Monthly aggregated report

On the 14th business day of the following month, CSDs shall provide the monthly aggregated report (see chapter 7 ).

This report shall include, per currency and party, the bilateral net amounts of the penalties against each of its counterparties (per CSD for cross-CSD fails), computed for all the business days of the previous month.

### 11.3.3    Payment pre-advices

In regard to the timeline of the collection and redistribution process, the payment pre-advice is to be issued by the CSD on the 15th business day of the following month[60].

### 11.3.3.1    Via Cash messages

OPEN ITEM ECSDA: shall pre-advices be issued by CSDs as well for credits to the CSD participants ?

For the cash messages, the mandatory fields are:

- Cash Account number of the participant (including CSDs) to be debited or credited;
- Cash Account number of the CSD dedicated to the penalties management (if applicable);
- Amount to be paid (= debit amount) / Amount to be received (= credit amount);
- Currency;
- Value date of relevant payment; and
- Free text (payment reference, reference to the penalty process, or other).

---

[59] T2S and SWIFT confirmed on 26.03.2019 the presence of all the information listed in these bullets in the future ISO 20022 semt.044 and ISO 15022 MT537/ 548 messages.

[60] Payment pre-advice messages are not (e-)invoices. Therefore, they shall not contain the elements listed in Article 6 of EC Directive 2014/55/EU as not to be perceived as such.

As indicated, a payment pre-advice message will contain only one amount. That means that the CSD will send out to every participant payment pre-advices only in case there are payments to be processed and, for any of the two possible payment directions (debit and credit), there will be a dedicated pre-advice (i.e. a payment pre-advice message can contain only a credit or a debit amount, but not both).

### 11.3.3.2   Via Settlement messages

Various Settlement messages can be used to report the net amount to be received/ paid, such as the following:

- settlement instructions;
- statement of transactions;
- status advice etc.

Settlement messages will be sent for both, the debit and credit amounts.

The Settlement message may contain one or several amounts depending on the type of message to be used (i.e. a statement may contain several amounts).

# 12 MISCELLANEOUS

## 12.1 CUTOVER PROCESS

Cash penalties will only be applied as from the business day where the penalty mechanism is implemented, i.e. there will be no late matching fail penalties applied for business days before the implementation date. Penalties should be computed considering the fails that occur on or after the activation date of the Penalty Mechanism.

<mark>Subject to regulators´ toleration</mark>, ECSDA CSDs agreed that the activation date for applying CSDR compliant penalties shall be aligned with the one of T2S, i.e. penalties shall start to be applied as of settlement date 23<sup>rd</sup> November 2020 (tbc.).

**SEFPs** (Settlement Fail Penalties) will be computed **for instructions that fail to settle on and after the activation date.**

**LMFPs** (Late Matching Fail Penalties) will be computed **for instructions matched on and after the activation date.**

Main principles:

- No SEFP or LMFP applies for a business day prior to the activation date.
- In case an instruction with ISD prior to the activation date is matched in the settlement system on or after the activation date, the CSD will compute a LMFP. Nevertheless, in the computation of this LMFP, the CSD will not consider the business days prior to the activation date.

See Annex V for examples.

## 12.2 CONTINGENCY AND EXCEPTIONS HANDLING

### 12.2.1 Delayed delivery of CSD reports

In case a CSD cannot deliver a scheduled report on time (see chapter 2), it shall inform its participants as soon as possible about this temporary operational disruption via the standard CSD customer communication means (the same applies in case of delayed payment processing).

### 12.2.2 Exceptional situations where the cash penalty mechanism should not be applied

In addition to situations where insolvency proceedings are opened against the failing participant, cash penalties should not be applied in the following situations where settlement cannot be performed for reasons that are independent from the involved participants:

i.      ISIN suspension from settlement due to a reconciliation issue;
i.      ISIN suspension from trading[61];

---

[61] This is not a legal obligation but just a possibility provided by ESMA.

ii.   settlement instructions involving cash settlement outside the securities settlement system operated by the CSD if, on the respective day, the relevant payment system is closed for settlement;

iii.  technical impossibilities at the CSD level that prevent settlement, such as: a failure of the infrastructure components, a cyber-attack, network problems.

CSDs should report the concrete cases falling in the above-mentioned categories to their competent authorities, and the competent authorities should have the possibility to ask the CSDs to apply cash penalties in the future in similar cases, if they consider the non-application of penalties unjustified.

## 12.3  CCP-RELATED ASPECTS – UNDER DISCUSSION WITH EACH

### 12.3.1   CSD participants that are CCPs[62]

Regarding penalties related to participants that are CCPs, the CSDR Standards stipulate that CSDs shall calculate and report penalties but not actually charge/ credit the calculated penalties.

As a result, such failed CCP settlement transactions will as well be excluded from the daily/ monthly net amounts calculations.

WORKING ASSUMPTION (EACH, ECSDA discussion ongoing): In order to apply a harmonised approach for T2S and non-T2S transactions, CSDs may apply a table listing all CCP BICs (such table is used already by T2S today and will be checked by EACH for completeness); this table may need to be enriched e.g. with LEI or other data to allow mapping against CSD participants´ (proprietary format) account data maintained by a CSD to identify transactions that involve a CCP and require special treatment and reporting. Thereby, CCP transactions that are not related to the CCPs´ clearing member business can be eliminated (as e.g. a separate CCP BIC outside the mapping table shall be used in such cases).To illustrate better the application of the general non-charging principle for CSD´s CCP penalty matters, following scenarios display on a more detailed level possible CSD, CCP, CSD participant, CCP clearing member and cross-CSD interactions in regard to which entity is collecting and redistributing penalties in question.

|  | Instruction X | Instruction Y |
|---|---|---|
| **Scenario 1- both instructions of a transaction belong to the same CCP** | | |
| Owner of the instruction | CCP A as CCP | CCP A as CCP |
| Entity to be charged | CM A of CCP A | CM B of CCP A |
| Charging entity | CCP A | CCP A |
| **Scenario 2- one instruction belongs to the CSD participant and the other to a CCP** | | |
| Owner of the instruction | CCP A as P | P A as P |
| Entity to be charged | CM A of CCP A | P A as P |
| Charging entity | CCP A | CCP A |

[62] CSDR requests this information to be provided by the CSD participants when applicable; in case the information is not provided for a CCP-cleared instruction, penalties will be calculated and charged by the CSD.

| Scenario 3- one instruction belongs to CCP A and the other to CCP B, both participants of CSD A | | |
|---|---|---|
| Owner of the instruction | CCP A as P | CCP B as P |
| Entity to be charged | CM A of CCP A | CM C of CCP B |
| Charging entity | CCP A directly with CCP B | CCP B directly with CCP A |
| **Scenario 4- one instruction belongs to CCP A as participant in CSD A (issuer CSD) the other to CCP B as participant of CSD B (investor CSD)** | | |
| Owner of the instruction | CCP A as P | CCP C as P |
| Entity to be charged | CM A of CCP A | CM E of CCP C |
| Charging entity | CCP A directly with CCP B | CCP B directly with CCP A |

*Table 1- CCP scenarios*

**\*CCP**= Central Clearing Counterparty
CM= Clearing Member of a CCP
CSD= Central Securities Depository; acts in capacity as a CCP (where relevant RTS articles apply) and also in capacity of a Participant of CSD
P= Participant of a CSD
Charging entity= entity collecting and also redistributing moneys (i.e. handling credit and also debit payments)

Hence, CSDs shall exclude from their collection and distribution processes the amounts due to be paid and entitled to be received by a CCP that is a CSD participant[63] and for which the related BIC is part of the "CCP BICs table".

### 12.3.2   Penalties calculation and collection process for CCPs

Related to Chapter 12.3.1, the CSD shall ensure that CCPs are provided with the calculation but not actually charge or distribute the penalties.

As such, in the CSD processes, CCP instructions will be included and flagged as such in:

- the computation (for daily calculation);
- the daily reporting;
- the monthly aggregated reporting.

The CSD will <u>not</u> include the CCP activity in the following processes:

- reporting of the amount to be paid and to be received; and
- actual credit or debit payments execution.

Depending on the CCP netting model, CCPs may regularly cancel all failing instructions after the last settlement cycle has finished.

Such CCP-cancellations after the cut-off do not affect the obligation for the calculation of the penalty by the CSD and, subsequently, the CCPs´ penalties processing towards its clearing members, i.e. such (cancelled) failed instructions shall still be considered by CSDs for penalties calculation and reporting to the settlement parties.

<mark>OPEN ITEM ECSDA:</mark>

---

[63] This was informally discussed with ESMA at the settlement discipline workshop on 5 June 2018.

According to CSDR RTS Art. 19 (d), CCPs shall report to CSDs the amounts they collected and distributed on a monthly basis. EACH and ECSDA agreed that ECSDA will provide a template (word, excel or similar) that shall be used by CCPs to report the required information (via Email, website upload/ entry or other means defined by the CSD).

# ANNEXES

## ANNEX I- T2S DOCUMENTS

1. T2S Penalty mechanism:

t2s penalty
mechanism.pdf

2. T2S CR654:

https://www.ecb.europa.eu/paym/target/t2s/governance/html/changerequests.en.html

3. Penalty lists – Draft message (20022) overview (version dd. 16.04.2019)

20190522_DraftMess
ageOverview_CR654_

4. List of T2S CSDR TF items for clarification sent to ESMA:

2017-06-28 - List of
CSDR Items for clarif

## ANNEX II - OTHER DOCUMENTS AND REFERENCES

1. Link to ESMA website re. CSDR:

https://www.esma.europa.eu/regulation/post-trading/settlement

2. CFI code mapping table (T2S CSDR TF version dd. 31.08.18):

2018-08-31
CFI_CSDR_mapping D

3. [ECSDA list of clarifications for ESMA to be added]

4. Penalties adjustments reason codes:

   a. Reason codes for penalty removal (as proposed by T2S, 08.04.2019, based on ESMA CSDR Q&A section "Settlement Discipline Questions 4 – Cash penalties: scope"):
      i. INSO – Insolvency
      ii. SESU – Settlement Suspended
      iii. SUSP – Trading status suspended
      iv. SEMP - Settlement on multiple platforms (applies in case the cash settlement is outside the CSD settlement system and the payment system is closed)
      v. TECH – Technical impossibilities
      vi. OTHR – any other case (requires a narrative text to be added)
   b. Reason codes for penalty reintroduction [to be added when available]
   c. Reason codes for penalty re-allocation [to be added when available]

## ANNEX III - SETTLEMENT SCENARIOS

### 1. Non-T2S CSDR SD penalties scenarios

Doc1 - Non-T2S
CSDR SD penalties s

### 2. T2S CSDR SD penalties scenarios

Doc2 -T2S CSDR
SDR scenarios- upda

## ANNEX IV - LIST OF CSDS USING THE FRAMEWORK AS MARKET PRACTICE

[To be filled in at a later stage]


## ANNEX V – CUTOVER PROCESS EXAMPLES (SEE FRAMEWORK CHAPTER 12.1)

*Note: the examples are based on the assumption that the activation date is, for instance, Monday 16 November 2020.*

**Example 1**
- A DVP settlement instruction enters and is matched in the settlement system at 10:00 on its ISD (Friday 13 November 2020):
    - The CSD will not compute the SEFP if the instruction fails to settle on Friday, 13 November 2020 because it is before the activation date.
- However, if the instruction fails to settle again in the settlement system on Monday, 16 November 2020 ("ISD+1" for the instruction), then the CSD will compute a SEFP:
    - This SEFP is computed because Monday, 16 November is the day of activation of the Mechanism. The SEFP will be computed and reported together with all penalties for Monday, 16 November 2020, i.e. on the daily reporting.

**Example 2**
- A DVP settlement instruction enters and is matched in the settlement system at 14:00 on Friday, 13 November 2020. The instruction has ISD Thursday, 12 November 2020 (i.e. enters and is matched in the settlement system one day after its ISD):
    - The CSD will not compute a LMFP for this instruction because the matching date (Friday, 13 November 2020) is before the activation date.
- If (on top of arriving one day late) the instruction also fails to settle in the settlement system on Friday 13 November 2020 (i.e. on "ISD+1" for the instruction):
    - The CSD will not compute the SEFP because the instruction fails to settle in the settlement system on Friday, 13 November 2020, which is before the activation date of the Mechanism.
- If the instruction fails again to settle in the settlement system on Monday, 16 November 2020 ("ISD+2" for the instruction), then the CSD will compute a SEFP:
    - This SEFP will be computed because Monday, 16 November is the day of activation of the Mechanism. The SEFP will be computed and reported together with all penalties for Monday, 16 November 2020, i.e. on the daily reporting.

**Example 3**
- A DVP settlement instruction enters and is matched in the settlement system at 14:00 on its ISD Monday, 16 November 2020:
    - The CSD will compute the SEFP if the instruction fails to settle on Monday, 16 November 2020, because it is the activation date.

The SEFP will be computed and reported together with all penalties for Monday, 16 November 2020, i.e. on the daily reporting.
- If the instruction fails again to settle in the settlement system on any following day, the CSD will compute related SEFPs.

**Example 4**
- A DVP settlement instruction enters and is matched in the settlement system at 14:00 on Monday, 16 November 2020. The instruction has ISD Friday, 13 November 2020 (i.e. enters and is matched in the settlement system one day after its ISD):
    - The CSD will compute a LMFP for this instruction because the matching date (Monday, 16 November 2020) is the activation date.

In the computation of this LMFP, the CSD will not consider the days prior to the activation date because the securities subject to penalties will have valid from equal to Monday, 16 November 2020. Therefore, in this example, the CSD will consider that there is no applicable business day for this LMFP.
- If (on top of arriving one day late) the instruction also fails to settle in the settlement system on Monday, 16 November 2020 ("ISD+1" for the instruction):
    - The CSD will compute the SEFP because the instruction fails to settle in the settlement system on Monday, 16 November 2020, which is the activation date of the Mechanism. The SEFP will be reported on Tuesday 17 November 2020.

**Example 5**
- A DVP settlement instruction, enters and is matched in the settlement system at 14:00 on Tuesday, 17 November 2020. The instruction has ISD Friday, 13 November 2020 (i.e. enters and is matched in the settlement system two business days after its ISD):
    - The CSD will compute a LMFP for this instruction:

In the computation of this LMFP, the CSD will not consider the days prior to the activation date because the securities subject to penalties will have valid from equal to Monday, 16 November 2020. Therefore, in this example, the CSD will consider only one business day for the LMFP (i.e. the LMFP will apply just for Monday, 16 November 2020).
The LMFP will be computed and reported on the daily reporting.
- If (on top of arriving two days late) the instruction also fails to settle in the settlement system on Tuesday, 17 November 2020 ("ISD+2" for the instruction):
    - The CSD will compute a SEFP because Tuesday, 17 November 2020 is after the activation date of the mechanism. This additional penalty will be reported on Wednesday 18 November 2020.