



EUROPEAN CENTRAL BANK

EUROSYSTEM

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Target2-Securities

Getting ready for CSDR

Monte Titoli 02 December 2019

Overview

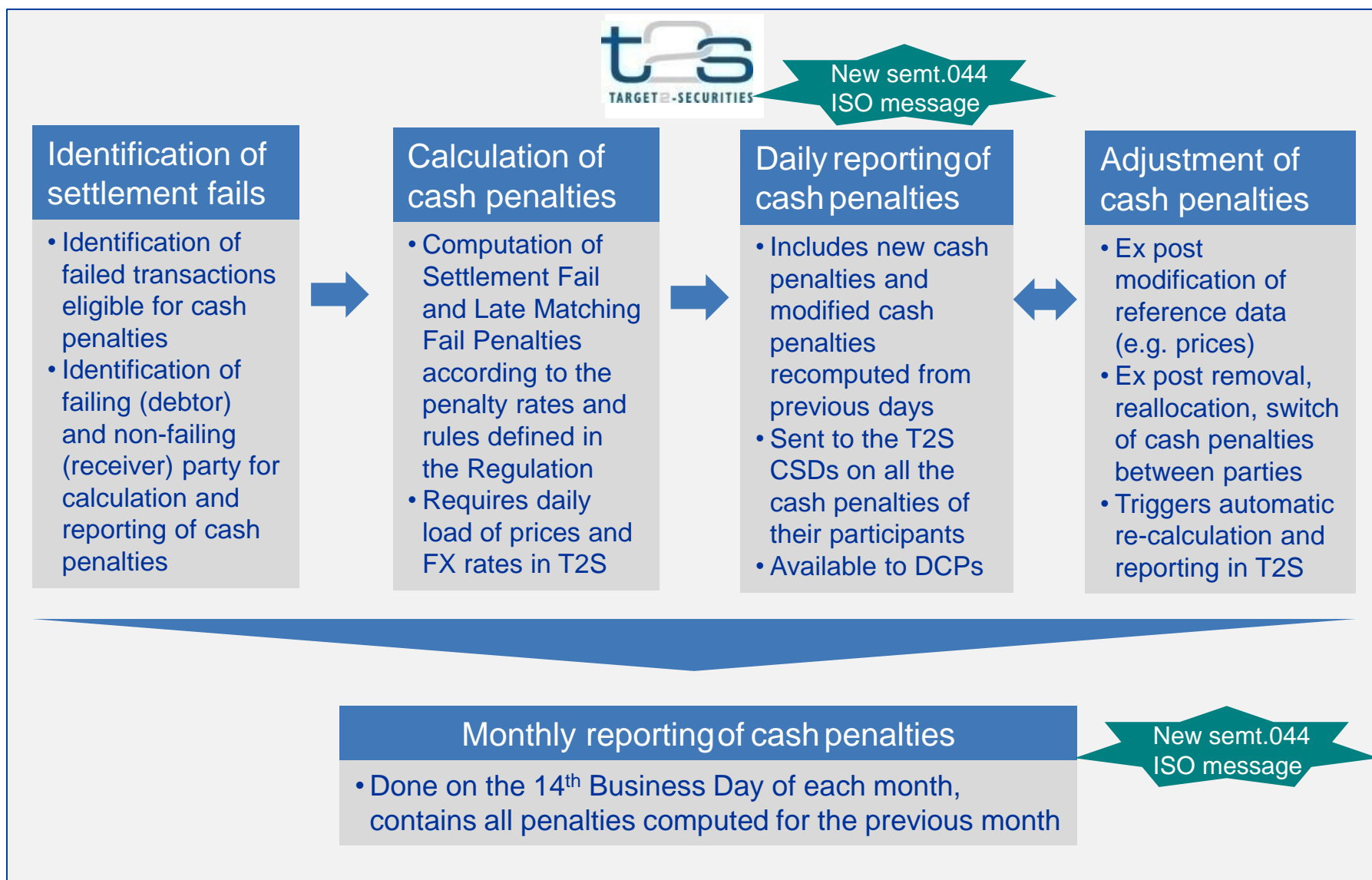
1 Implementation of the settlement penalties mechanism in T2S

2 Focus on settlement efficiency in T2S

Background

- The T2S CSDR Task Force (TF) was established by the T2S Steering level in February 2016, in order to identify the necessary changes to the T2S platform resulting from the CSD Regulation (CSDR), with the objective to facilitate T2S CSDs' timely compliance to CSDR
- The main focus of the CSDR TF has been the design of the T2S penalty mechanism which is reflected in the Change Request 654 published on the ECB website ([CR654, additional documentation](#))
- In order to ensure that the T2S penalty mechanism fully complies with CSDR requirements, the CSDR TF working assumptions and regulatory interpretation of the CSDR articles were communicated and validated on a regular basis with Regulators prior to be translated into user requirements
- This good cooperation with Regulators has allowed to stabilise the scope of the T2S penalty mechanism and authorise the implementation of CR654 for November 2020 only 4 months after the final Regulatory Technical Standards on Settlement Discipline were published in September 2018

Scope of the T2S penalty mechanism



Out of scope of the T2S penalty mechanism

- As decided by the CSDR TF, the **collection and re-distribution of cash penalties** (collecting payment from the failing participants, and re-distributing the proceeds to the participants that suffered from the settlement fails) is managed by CSDs **outside the scope of T2S penalty mechanism**
- While it was initially considered to use a mechanism allowing direct debit such as Target2, as per latest discussions in the CSDR TF, **T2S CSDs are considering using Payment Free of Delivery (PFOD) settlement instructions in T2S**, currently mainly used for the settlement of Corporate Actions in cash, for some or all of the payment flows related to cash penalties. The assumption is that this process will fully **rely on existing T2S functionalities**
- The buy-in process, where the CSD plays a limited role, is outside the scope of the T2S penalty mechanism
- Cash penalties topics which are not covered by the T2S penalty mechanism and/or related to non T2S-CSD are documented in the **Draft ECSDA CSDR Penalties Framework** ([link](#))

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Workshop on Market Settlement Efficiency (MSE)

CSDs in T2S set up a focus group to:

- Understand the factors underlying the current settlement efficiency/fails
- Identify possible enhancements in T2S which could contribute to increasing settlement efficiency (e.g. functional or technical improvements of the T2S platform, or changes to CSDs and their customer's behavior/practices)

Methodology

Two settlement efficiency indicators were used/introduced:

- **The Platform Settlement Efficiency Indicator (PSEI)**, to assist in determining whether T2S is performing as expected from a platform perspective;
- **The Market Settlement Efficiency Indicator (MSEI)**, for a market-oriented approach, determining whether business objectives are being met and to assist in the setting of realistic targets for settlement efficiency. Includes “party on hold” transactions

From November 2019, both those indicators will disappear from the T2S Operations Report and will be replaced by a new unique settlement indicator → **DATF-Settlement Efficiency (DATF-SE)**. With the new methodology the Party on Hold instructions are included as unsettled in the calculation.

Workshop on Market Settlement Efficiency (MSE)

- T2S Global figures for the two indicators in September 2019 at EOD:
 - In volume PSEI: 97.03% vs MSEI: 93.68%
 - In value PSEI: 97.91% vs MSEI: 94.20%

Thus proving that the high fail rates are independent of the T2S platform and are instead related to:

- Party On Hold instructions
- Lack of securities

Those two components together are responsible for approximately 90% of the EOD fail rate

Aged transactions

CSG took a deep dive into the monitoring of “aged transactions”

- 80% have a “Party on hold” status
- Relevant to the cash penalty mechanism as from its activation date, (i.e. November 2020)
- The current assumption is that aged transactions is relevant for the buy-in as well

02/01/2019		
Period	# Unsettled	# Inxs
< 01 Mth	79 888	1 230 418
Total	118 076	1 269 854

01/04/2019		
Period	# Unsettled	# Inxs
< 01 Mth	81 495	1 214 838
Total	106 362	1 240 383

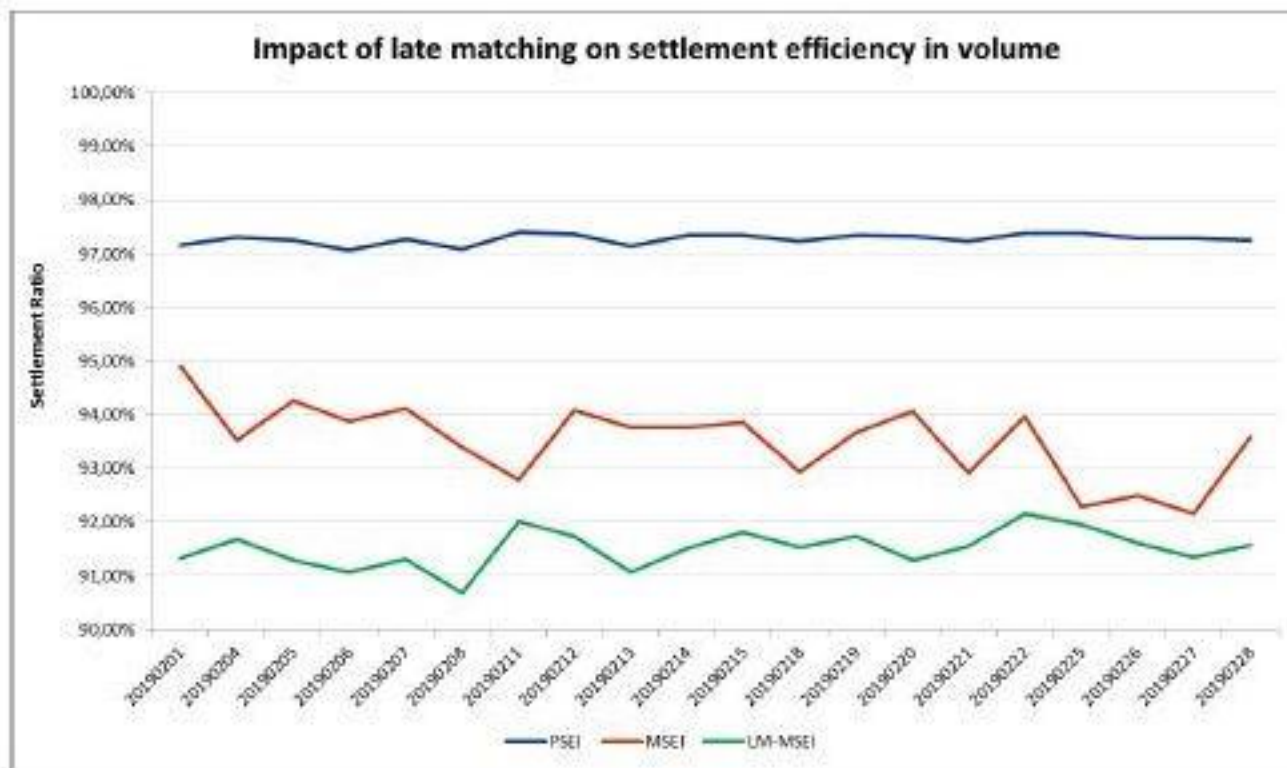
01/10/2019		
Period	# Unsettled	# Inxs
< 01 Mth	67 095	1 135 219
Total	95 213	1 163 904

Currently matched settlement instructions are recycled forever in T2S. CSG is discussing whether *CR 691 - Recycling period of 60 days for matched instructions* should be implemented

- Potential improvement of the T2S settlement efficiency ratio in volume up to ~1.67% if > 3 months (60 days) is configured
- Monitoring of statistics in October 2019 have shown a decrease of total of unsettled instructions due to clean-up actions by CSDs/market participants
- However, the total of unsettled instructions remains high and the clean-up actions are not sufficient to offset the continual volume of instructions presented for settlement within T2S coupled with the usual observed fail rates

Late matching transactions

- Late matching relevant in CSDR context – will attract penalties – but is not measured
- ~ 2.4% potential negative effect on settlement efficiency in volume
- CSDs to initiate/continue analysis and dialogue with the participants on late matching



CR-653 – Partial Release

On 16 November 2019, Change Request T2S-0653-URD has been deployed in T2S as part of Release 3.2, thus introducing a new functionality in T2S, Partial Release

- Unlike the previous Release functionality, which applied at instruction level for the full quantity, the new Partial Release functionality allows to release instead only part of the instruction (for the eligible transactions)
- Benefits are expected in terms of Settlement Efficiency as the functionality gives the possibility to increase the amounts settled

Thank you for your attention!

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Annex: Overview of T2S penalty mechanism (CSDR)

Timeline

