

# Penalties application model

MODEL DESCRIPTION  
RELEASE 1.1 - AUGUST 2011

## INTRODUCTION

Consob and the Bank of Italy's settlement service regulation require Monte Titoli participants to guarantee the availability of cash and securities necessary to finalise settlement of transactions with their counter-parties. This in addition, will allow Monte Titoli to improve the efficiency of the settlement system.

A penalties model has been developed to encourage participants to comply with this requirement. For this reason full details of the penalties model have been made available on this document.<sup>1</sup>

Should the settlement cycle not be finalized within the default timetable, Monte Titoli will evaluate the causes, and determine whether or not penalties should be applied. Please note, that participants will be provided with adequate information should they incur in any penalties.

### 1. Penalties for delay in cash payment during the intraday net settlement cycle

*(This model has been in force since February 2007)*

Any delays in cash payments on a debit position during the intraday net settlement cycle resulting from a participant's action, and keeping the cycle from finalizing within the expected deadline, incurs in penalties. The rationale behind this policy is to deter this type of actions and avoid their negative impact on the settlement system.

Currently, starting at 11.45 AM participants are notified of their cash balance by means of message G32. If they are in a debit position, they are required to make funding arrangements within 1 hour after the notification has been received, as detailed in Monte Titoli settlement service regulation. In the case that the participant is unable to meet its obligation within the specified deadline, a penalty is charged.

The penalty is determined on the basis of two elements one is fixed, while the other is floating. The fixed component is determined by taking into consideration the frequency of cash payment delay experienced by the participants during the year and the quantification of delay, while the floating component is calculated as 10 basis points, on a daily basis (yearly basis 360 days), on the debit cash balance delayed.

All parameters considered to determine the penalty are detailed in the following chart:

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<sup>1</sup> Penalties are charged irrespective of requests of securities in Securities Lending and Borrowing system operated by Monte Titoli.

*Table 1*

Flat fee - in Euro				
N. of delays	Delay (in minutes)	1 - 15 min	16 - 30 min	31 - up
	First		500	2,000
Second		1,000	4,000	8,000
Third and greater		2,000	8,000	16,000
Fee interest (in bps)		10 bps		

Monitoring is performed by Monte Titoli on a daily basis and, in event of delay, the penalty is clearly identified on the invoice sent to the participant in the month where the delay was experienced.

## 2. Penalties for delays in the delivering of securities at the end of the day

*(this model will enter into force on 1<sup>st</sup> September 2011 and will replaces the current one)*

Penalties will be applied to all positions in which there is a lack of securities at the closing of RTGS system (currently at 6.00 PM) irrespective of Intended Settlement Date.

Proceedings from penalties will be distributed amongst participants who are in a credit position during the same business day, on the affected ISIN codes; payment of penalties and their distribution will take place as detailed in section 5.

The model is subject to the below detailed rules.

### 2.1 Determination of securities positions subject to penalties

Penalties are charged, per each settlement account of the participant and per single ISIN code, on the counter-value of the balance of all unsettled transactions<sup>2</sup> during the day and remaining open in the RTGS system.

To determine the multilateral balance of the unsettled transaction at the end of the business day, the following criteria are applied:

<sup>2</sup> All unsettled transactions are considered: transactions unsettled in the net cycles, OTC transactions and on exchange transactions sent to the gross settlement cycle (for example the spot leg of overnight repo - PCT)

- unsettled transactions due to lack of securities and still open after the closing of RTGS system (currently at 6.00 PM) are included
- the available balance (excluding eventual blocks) on the settlement account<sup>3</sup> is tracked
- for each securities account and each ISIN code, the multilateral balances (SMT) subject to penalty charge are calculated as detailed below:

*SMT subject to penalty (if < 0) =  $\Sigma(\text{deliveries}) + \Sigma(\text{withdrawals}) + \text{availability in the account at 6.00 PM}$*

The multilateral balance is evaluated as detailed below:

- a. in the case of securities traded on exchange: Market price on the preceding day will be used as reference
- b. in case of securities traded off exchange (or in the event that the price is not available) the nominal value will be used.

the following percentages will be applied to the multilateral balances subject to penalties<sup>4</sup>:

- c. 0,001% for bonds (either corporate and government)
- ci. 0,02% for all the other securities (shares, warrant, ETF).

Exemptions on penalty charges per single ISIN code will apply if the amount<sup>5</sup> is less than:

- € 5.000.000<sup>6</sup> of counter-value for bonds;
- € 250.000<sup>7</sup> of counter-value for the other securities.

## 2.2 Positions in bonis (credit positions)

As mentioned above, proceedings from penalties will be distributed amongst participants “in bonis”, this meaning participants maintaining an unsettled net credit position on the same ISIN codes on which penalties have been charged.

This bonus will be paid on the counter-value of all unsettled transactions<sup>8</sup> during the day and those remaining open in the RTGS system.

Multilateral balances of transactions appearing as unsettled at the end of the day will be determined as follows:

- unsettled positions due to lack of securities are registered after the closing of RTGS system (currently at 6.00 PM)

<sup>3</sup> The balance on the account is considered, in order to avoid charging penalties to participants with either delivery and withdrawal positions in the same ISIN code, but with different amounts.

<sup>4</sup> Percentages may be revised by Consob and Bank of Italy

<sup>5</sup> Amounts may be revised by Consob and Bank of Italy

<sup>6</sup> Nominal value is considered for non listed securities or when price is not available. For securities issued in currency other than EUR, the official exchange rate of the preceding day is considered.

<sup>7</sup> If price is not available and for non listed securities the nominal value is considered; exception is made for warrants and covered warrants, so that if not listed or the price is not available, a conventional value of 0,30 EUR is applied (the same in use to calculate centralization feed due to Monte Titoli).

<sup>8</sup> All unsettled transactions are considered: transactions unsettled in the net cycles, OTC transactions and on exchange transactions sent to the gross settlement cycle (for example the spot leg of overnight repo - PCT)

- for each securities account and each ISIN code, multilateral balances “in bonis” are calculated according to the following rule::

*SMT in bonis (if > 0) =  $\Sigma(\text{deliveries}) + \Sigma(\text{withdrawals})$*

The multilateral balance is evaluated as detailed below:

1. For exchange-traded securities: closing market price of the preceding day will be used as reference;
2. For securities traded off-exchange (or in the event that prices are not available) the nominal value will be used.

Bonus distribution will take place according to the rules described in section 3 and the timetable detailed in paragraph 5.

### **3. Distribution of penalties generated funds**

Distribution to the elected counter-parties will be calculated on a daily basis, proportional to the counter-value owned by each counter-party in respect of the total counter-value, per ISIN.

Should penalties not be charged, due to the exclusions described in paragraph 2, no distribution will place.

It has been determined that 94%<sup>9</sup> of funds generated through penalties will be distributed amongst in bonis participants; 6% of penalties will be retained by Monte Titoli (for an amount not exceeding 150.000,00 EUR on yearly basis) to cover costs related to the operation of the penalty system. Any remaining amounts will be donated to charity.

### **4. Notifications**

Participants will receive, on a daily basis, a report detailing positions subject to penalties and positions subject to distributions.

The report will be submitted electronically to the addresses provided by the participants.

### **5. Settlement of debit and credit amounts**

All amounts calculated according to the rules detailed in paragraph 2 and 3 will be recorded 2 months after the event has taken place. For example, amounts determined and calculated in September will be settled in November.

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9 At the beginning of the year, Monte Titoli provides to notify electronically to its participants in the settlement system the percentage of distribution of charged penalties. For the period in-between 01/09/2011 and 31/12/2011 100% of penalties will be distributed.