
**EACH Response – European Commission
legislative proposal on CSDR Refit**

May 2022

1. Introduction

The European Association of CCP Clearing Houses (EACH) represents the interests of Central Counterparties (CCPs) in Europe since 1992. CCPs are financial market infrastructures that significantly contribute to safer, more efficient and transparent global financial markets. EACH currently has 18 members from 14 different European countries. EACH is registered in the European Union Transparency Register with number 36897011311-96.

EACH appreciates the opportunity to provide feedback to the European Commission legislative proposal to amend Regulation (EU) No 909/2014 (henceforth "*the legislative proposal*").¹

¹ https://ec.europa.eu/finance/docs/law/220316-csdr-review-proposal_en.pdf

2. Executive Summary

EACH welcomes the initiative of reviewing the CSDR Settlement Discipline Regime (SDR) as part of the CSDR Refit process.²³ As demonstrated by the number of the questions raised by market participants on this matter (such as ESMA Q&As)⁴, the CSDR SDR, while well intended, could benefit from different clarifications. EACH particularly welcomes several changes suggested by the European Commission, such as the ability for CCPs to recover losses from imbalances, and the fix applied to penalty rates in the context of negative interest rates.

Overall, EACH does not have any major objections or issues with the legislative proposal published by the European Commission. Our main point is highlighting the gap left by the removal of Mandatory Buy-in (MBI) regime for the special case of CCP cleared share transactions.

Regarding the proposal on delayed MBI regime, EACH supports that any potential provisions imposed by the Commission on mandatory buy-ins avoid the 'one-size-fits-all' approach (e.g. differentiating across asset classes; dealer structures, etc.). Furthermore, we consider it important to account for how the settlement discipline-related post-trading picture interrelates with the trading picture (e.g., the effects of internalised settlement volumes).

Lastly, EACH make several suggestions that aim to provide operationally important changes for CCPs. These can be briefly explained as:

- **SME Growth Markets extension period – (new) Article (7)(3) CSDR:** We had previously requested for this to be amended to "15 business days" – it has consequently been amended to 15 calendar. EACH politely requests this is amended to "15 business days".
- **Introduction of a 'pass-on mechanism' – (new) Article 7(3)(a) CSDR:** We request that it is made clear in this article that it is subject to Article 10(a), and that a pass-on cannot be made to a CCP.
- **Factors not attributable to the participants – (new) Article 7(4) CSDR:** Regarding "reasons not attributable to the participants" and "transactions that do not involve two trading parties", EACH wondered why are these exempted from MBIs, but not if cleared by CCPs.
- **Consistency of Buy-in timeframes – Article 7(5) CSDR:** Having different/shorter extension periods specifically for cleared share fails will likely cause difficulty in pass-on timings along a chain involving cleared and uncleared fails, and risks also unduly de-incentivising central clearing. We therefore politely request the removal of Article 7(5).
- **Cash compensation – (new) Recital 7, (new) Article 7(7) CSDR:** We believe that Recital (7) should be amended to include a remedy for cash compensation, with an

² <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32014R0909>

³ <https://tinyurl.com/3ym3nbmn>

⁴ https://www.esma.europa.eu/sites/default/files/library/esma70-708036281-2_csd_r_qas_1.pdf

equivalent update to Article 7.7 as that for Article 7.6. We understand this update would be in line with the first two sentences of Recital (7) of the legislative proposal.

- **The applicability of the CCP exemption – (new) Article 7(11) CSDR:** CCPs are not always direct participants in CSDs, so we request that the first paragraph of article 7(11) is amended to remove “participants which are” such that it reads “Paragraphs 2 to 9 shall not apply to failing CCPs, except for transactions entered into by a CCP where it does not interpose itself between counterparties.”

We develop the above proposals in the following sections.

3. EACH feedback on the CSDR legislative proposal

a) Ability for the European Commission to introduce MBIs for specific instruments/transaction categories – (new) Article 2(a) CSDR

EACH would like to highlight that Article 15 of the Short Selling Regulation (SSR) has been removed via Article 72 CSDR.⁵ This removal came into force in February 2022, as per the provisions of Article 76(5) CSDR. We understand this was done on the basis that the mandatory buy-in of the special case of cleared share trades would then be covered under the umbrella of CSDR. This removal, combined with the delay of the MBIs regime leaves a gap in the regulation where MBIs for CCP cleared shares are concerned. In highlighting this, EACH notes its support for the continuation of the Buy-in provisions included in Article 15 SSR, and requests that the relevant authority ensures these provisions are reintroduced in the appropriate manner.

EACH also supports the European Commission and ESMA's analysis of the settlement discipline situation since the implementation of the settlement discipline regime, ensuring that any potential provisions on mandatory buy-ins avoid the 'one-size-fits-all' approach (e.g. differentiating across asset classes; dealer structures, etc.). Furthermore, EACH would also suggest that authorities consider how the settlement discipline-related post-trading picture interrelate with the trading picture, such as the effects of internalised settlement volumes.

b) EACH welcomes the capacity to recover losses from imbalances – (new) Article 7(2)(a) CSDR

EACH welcomes that the European Commission has introduced the capacity for CCPs to recover losses from penalties¹ imbalances, as per the new Article 7(2)(a) CSDR proposal.

c) SME Growth Markets extension period – (new) Article (7)(3) CSDR

The extension period for SME fails has been suggested to be changed from 15 days to 15 *calendar* days. However, as per our previous feedback, we believe this should be 15 *business* days to be consistent with the definition of the other extension periods

d) Introduction of a 'pass-on mechanism' – (new) Article 7(3)(a) CSDR

EACH notes that the European Commission has suggested introducing a pass-on mechanism with an explanation of how the pass-on mechanism will work in the new Article 7.3a. This describes the 'end receiving participant' in a chain executing a buy-in, with pass-ons being passed up the fail chain through the 'intermediate receiving participants'. However, where a CCP is the 'intermediate receiving participant' it is responsible for executing the buy-in (Article 10(a)).

⁵ <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:086:0001:0024:en:PDF>

We request that it is made clear in this article that it is subject to Article 10(a), and that a pass-on cannot be made to a CCP.

We kindly suggest that the consequences of this on the pass-on mechanism are also considered for those downstream of a CCP in a fails chain. Previous discussions between CCPs and their members on this point indicate this is a concern for other market participants as well.

e) Factors not attributable to the participants – (new) Article 7(4)

EACH would appreciate additional clarity on 'reasons not attributable to the participants' and 'transactions that do not involve two trading parties'. In particular, on why these should be exempted from MBIs, but not if cleared by CCPs.

f) Consistency of Buy-in timeframes – Article 7(5) CSDR

EACH does not see the benefit of having different/shorter extension periods specifically for cleared share fails. ~~It~~ This is likely to cause difficulty in pass-on timings along a chain involving cleared and uncleared fails. It may even unduly de-incentivising central clearing. We therefore kindly request the removal of Article 7(5).

g) Cash compensation – (new) Recital 7, (new) Article 7(7) CSDR

We note that the first two sentences of recital (7) in the legislative proposal recognise that the unequitable remedy of asymmetrical payments applies to both buy-ins and cash compensation.

(7) Mandatory buy-ins and cash compensation processes allow for the payment of the difference between the buy-in price and the original trade price to be made from the seller to the purchaser only where that buy-in or cash compensation reference price is higher than the original trade price. This asymmetry for the payment of the differential could create an unequitable remedy that would unduly benefit the purchaser in the event that the buy-in or reference price is lower than the original trade price.

The payment of the differential between the buy-in price and the original trade price should therefore apply in both directions to ensure that the trading parties are restored to the economic terms, had the original transaction taken place.

However, the final sentence only provides a remedy for the case of buy-ins, which has the associated update to Article 7.6.

If our understanding is correct, recital (7) should also include a remedy for cash compensation, with an equivalent update to Article 7.7 as that for Article 7.6.

h) The applicability of the CCP exemption – (new) Article 7(11) CSDR

To provide legal certainty and given that CCPs are not always participants of CSDs, EACH requests that the first paragraph of article 7(11) be amended to remove “participants which are” such that it reads “Paragraphs 2 to 9 shall not apply to failing CCPs, except for transactions entered into by a CCP where it does not interpose itself between counterparties.”

i) EACH welcomes the fix on Penalty rates in the context of negative interest rates – Article 7(14) CSDR

EACH thanks the European Commission for clarifying, in amending Article 7(14) CSDR, the issue of penalty rates in the context of negative interest rates.

New Article 7(14): *The Commission shall be empowered to supplement this Regulation by adopting delegated acts in accordance with Article 67 specifying parameters for the calculation of a deterrent and proportionate level of the cash penalties referred to in paragraph 2, third subparagraph of this Article based on asset type, liquidity of the financial instrument, type of transaction and the effect that low or negative interest rates could have on the incentives of counterparties and fails. The parameters used for the calculation of cash penalties shall ensure a high degree of settlement discipline and the smooth and orderly functioning of the financial markets concerned.'*

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