

CAPCO

CSDR SETTLEMENT DISCIPLINE

ON-GOING CONCERNS AND A REGULATORY REVIEW
– HOW READY ARE YOU?



INTRODUCTION

Market participants and industry associations continue to raise concerns about CSDR's Settlement Discipline Regime (SDR), casting doubts on the clarity of the current rules as well as their potential impact outside the sphere of securities trading and settlement. But with the SDR implementation date nearing, and the European Commission Review of CSDR and consultation for a CSDR REFIT progressing – how ready are firms for SDR go-live?

The European Commission recently endorsed the proposed delay to the implementation of the CSDR SDR to 1st February 2022. The SDR introduces several measures aimed at preventing and addressing failures in the settlement of securities transactions.

There remains a pronounced level of uncertainty around the implementation of the SDR. Market Participants and Industry Associations continue to voice concerns over specific aspects of the Regime, such as the impact of mandatory buy-ins on market liquidity and overall industry readiness. The recent targeted consultation on the review of the regulation has seen these concerns raised once again.

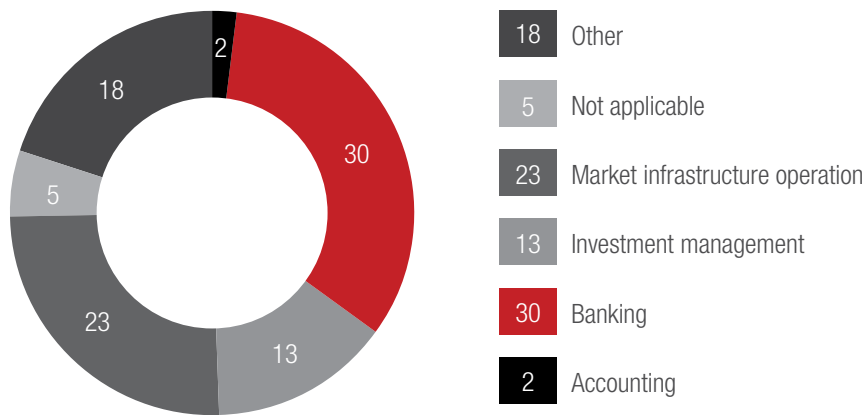
This ongoing uncertainty, and the prospect of potential legislative amendments to CSDR, call into question how ready firms are for the SDR's introduction in just over eight months' time.

TARGETED CONSULTATION ON THE REVIEW OF CSDR

A targeted consultation on the Review of CSDR took place from December 2020 through February 2021. The consultation covered all articles of the CSDR, including the SDR, and generated more than 90 contributions from a broad range of stakeholders (as shown in Figure 1).

The feedback highlighted a range of specific areas where targeted action may be necessary to ensure the fulfilment of the objectives of the CSDR in a more proportionate, efficient, and effective manner. This also considered the pressure put on markets by the COVID-19 pandemic. The consultation and a summary of responses can be found on the European Commission's [website](#).

Figure 1: Contributions to the Targeted Consultation on the Review of CSDR

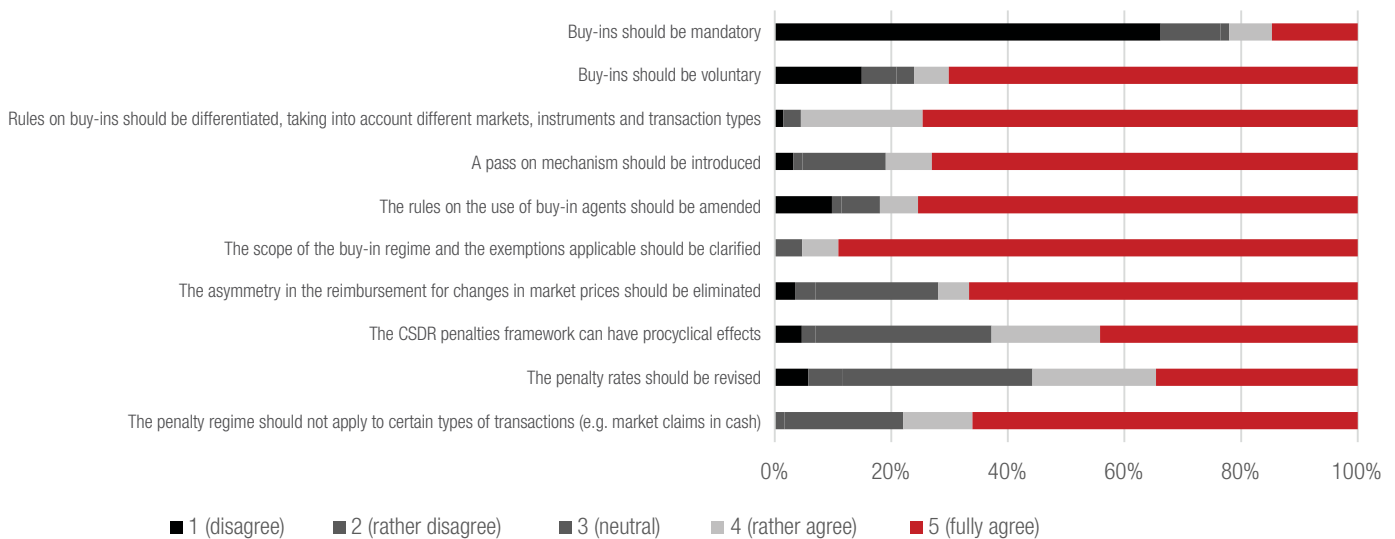


Source: European Commission 2021. Received contributions: Review of Regulation on improving securities settlement in the European Union and on central securities depositories. European Commission, viewed 9 April 2021. <https://ec.europa.eu/info/consultations/finance-2020-csdr-review_en>.

As expected, the current mandatory buy-in requirement of the SDR is widely felt to require a thorough reassessment as to its appropriateness. Figure 2 below captures responses to Question 34 of the Review of Regulation on improving securities settlement in the European Union and on central securities depositories. The key highlights drawn from stakeholder responses on the SDR (excluding blank responses and “Don’t know / No opinion” responses) are as follows:

- Most respondents agree that there is a need to revise the settlement discipline regimes (76% responded “Yes”).
- Most respondents either disagree (66%) or rather disagree (10%) that buy-ins should be mandatory.
- 95% of respondents either fully agree or rather agree that the scope of the buy-in requirement and applicable exemptions should be clarified.
- 96% of respondents either fully agree or rather agree that the buy-in rules should be differentiated to consider different markets, instruments, and transaction types.
- 81% of respondents either fully agree or rather agree that a pass-on mechanism should be introduced.
- 82% of respondents either fully agree or rather agree that the rules on the use of buy-in agents should be amended.

Figure2: Stakeholders' responses concerning the SDR
(excluding blank responses and "Don't know / No opinion" responses)



Source: European Commission 2021, Received contributions: Review of Regulation on improving securities settlement in the European Union and on central securities depositories, European Commission, viewed 9 April 2021, <https://ec.europa.eu/info/consultations/finance-2020-csdr-review_en>.

The European Commission is currently preparing a report for submission to the European Parliament and, if necessary, the European Council outlining proposed legislative changes. This is expected to be published during Q2 of 2021.

More recently, 16 trade associations in the European and global financial markets wrote a Joint Trade Associations letter to the European Commission and ESMA raising concerns about the implementation of the SDR mandatory buy-in requirement. The purpose of the letter was not to restate responses already submitted for the Review, but to highlight a critical timing issue in relation to the mandatory buy-in implementation schedule.

Any proposed legislative amendments to CSDR arising from the Review are not expected to emerge until Q4 2021. Given the significant global implementation effort required to support the mandatory buy-in requirement, including system development and global client outreach, the Associations have expressed a

concern that market participants will be required to proceed with their implementations despite lacking clarity on the scope or timing of the Review process.

The Joint Trade Associations Letter asks the European Commission for clarity on the Review and the implementation schedule for CSDR SDR mandatory buy-ins at the earliest opportunity to avoid redundancies in on-going implementation efforts and investments, as well as to avoid the need for repeat outreach programmes for global clients. The European Commission responded to this letter on 30th April 2021 to state that "no decision has been made on the changes that may be proposed as part of the Commission proposal to amend CSDR". The Commission will only be able to determine the concrete amendments to present for adoption by the co-legislators after a thorough impact assessment according to the Better Regulation Guidelines.

EUROPEAN COMMISSION CSDR REFIT ROADMAP

Between March 8 and April 5 2021, the European Commission conducted an impact assessment (roadmap details [here](#)) seeking views on how CSDs are working, focusing on:

- How CSDs can operate in different countries across the EU
- How requests to use their services are handled
- Whether there are other substantive barriers to completion in this sector that need to be addressed.

Based on those findings, the Commission may consider amending existing rules to simplify the CSDR with a view to developing a

more integrated post-trading landscape in the EU (CSDR Refit).

The aim of the CSDR Refit is to build on the conclusions of the Commission report on Targeted Consultation on the Review of CSDR. The impact assessment underpinning the roadmap will be prepared in parallel with the evaluation of the CSDR.

Although it is recognized that the rules under the SDR have not yet entered into force, many respondents used the feedback period of the CSDR Refit roadmap to highlight the importance of incorporating a review of the SDR mandatory buy-in requirement, as a priority, in the CSDR Refit. The summary of the responses can be found at the European Commission's [website](#).



WHAT'S NEXT FOR MARKET PARTICIPANTS?

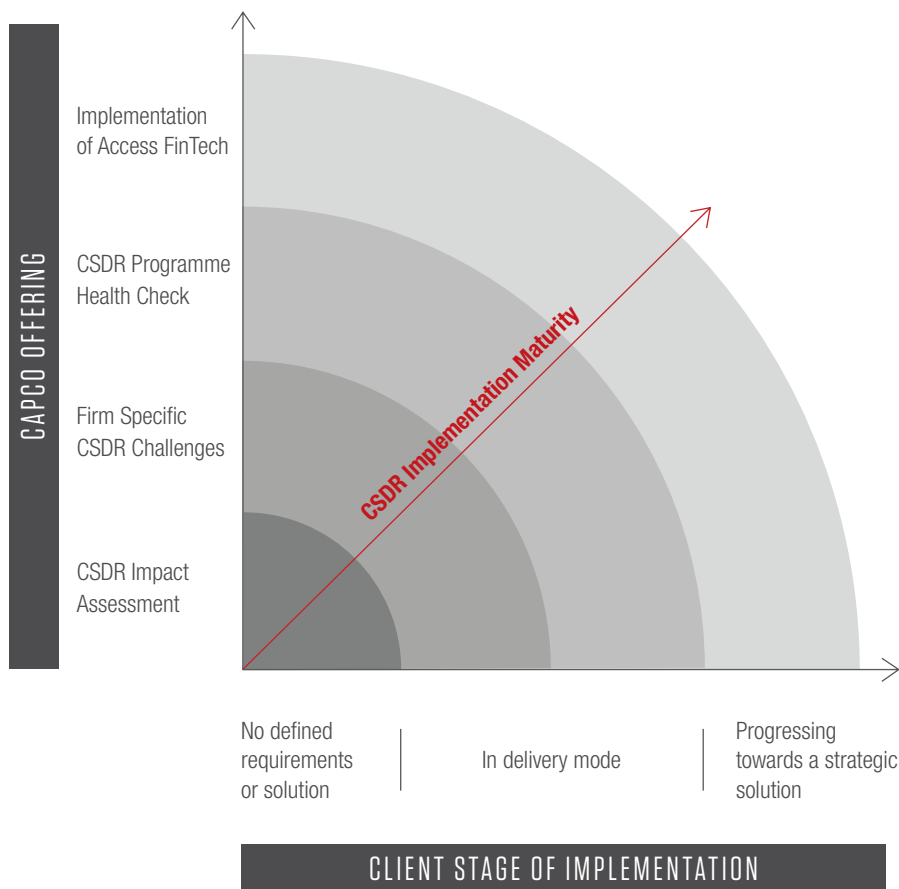
The ongoing concerns and the Review of CSDR should not lead market participants to halt or lose momentum around their implementation efforts. Even if a firm feels itself to be immature with respect to their requirement definitions and solution design, there is still time implement a minimum viable solution to be compliant.

For those already in delivery mode, firms should start to think more strategically about their solutions for cash penalties and mandatory buy-ins and what is essential to implement. Furthermore, we believe that market participants should look

across their post-trade processes – and more widely than just the management of settlement fails – to improve operational efficiencies and resolve legacy issues that in turn will address the requirements of CSDR.

We understand that firms are at different stages of the SDR implementation process, but wherever you are on that journey, Capco can help. We can apply our SME knowledge, delivery experience and accelerators to address CSDR requirements whether that be to help build a minimal viable product to be compliant, or to help you progress to a more strategic solution.

Figure 3: Client stage of the SDR implementation vs. Capco support available



HOW WE CAN HELP

1. CSDR Impact Assessments

The SDR will apply to all trading level parties regardless of location or jurisdiction, including any non-EU firms settling trades on EU (I)CSDs. If you are unsure whether CSDR applies to you, or whether you have not yet fully defined requirements or solutions, Capco can help. We can perform an impact assessment, build out requirements, create a delivery roadmap and provide recommendations for a solution design. We understand that market participants will be impacted differently by CSDR depending on their business model, product offering and legal entity structure, and can accordingly bring relevant expertise and approaches.

2. Firm Specific CSDR Challenges

Capco can support any firm that has specific CSDR related challenges arising from business models, solution design and programme maturity. Examples include client outreach preparation, mandatory buy-in operating model design and settlement efficiency initiatives.

3. CSDR Programme Health Check

Capco can help firms already in delivery mode, or firms that are refreshing their requirements after the regulation delay, through the provision of a programme QA and readiness assessment. This includes validation of requirements and regulatory text traceability, review of solution and process design as well as a review of your technology roadmap.

4. Implementation of Access FinTech

Capco is Access FinTech's Implementation Partner and can support firms adopting or assessing the feasibility to adopt Access FinTech's CSDR or Settlements module. We can support clients in vendor adoption including requirements gathering, data sourcing analysis, TOM design and platform configuration.

For any further details on our offerings, please contact Tej Patel, David Turmaine or Agnieszka Pokorska.

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ABOUT CAPCO

Capco is a global technology and management consultancy dedicated to the financial services industry. Our professionals combine innovative thinking with unrivalled industry knowledge to offer our clients consulting expertise, complex technology and package integration, transformation delivery, and managed services, to move their organizations forward.

Through our collaborative and efficient approach, we help our clients successfully innovate, increase revenue, manage risk and regulatory change, reduce costs, and enhance controls. We specialize primarily in banking, capital markets, wealth and asset management and insurance. We also have an energy consulting practice in the US. We serve our clients from offices in leading financial centers across the Americas, Europe, and Asia Pacific.

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