

MEMO# 34172

June 2, 2022

ICI Global Comment on the Central Securities Depositories Regulation

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TO: ICI Global Members SUBJECTS: International/Global
MiFID, EMIR, AIFMD, UCITS V RE: ICI Global Comment on the Central Securities Depositories Regulation

On March 16, 2022, the European Commission (Commission) proposed the review of the Central Securities Depositories Regulation (CSDR).[\[1\]](#) The review of CSDR was included in the Commission's 2021 Regulatory Fitness and Performance program (REFIT).[\[2\]](#) ICI Global previously advocated on the settlement discipline regime (SDR), including calling for the removal of the mandatory buy-in regime (MBR) in a response[\[3\]](#) to a prior Commission consultation and industry coalition letters in March and July last year.[\[4\]](#)

In late May, ICI Global submitted a paper to the Commission recommending the removal or substantial reform of the MBR as it would, contrary to the goals of CSDR, fail to increase the safety and efficiency of securities settlement and settlement infrastructures. The letter asserts that introducing the MBR would have various negative consequences for market participants, including fund investors:

- reduce liquidity, especially for less liquid securities, thus increasing investor risk and cost;
- force non-failing counterparties to accept cash in lieu of securities even if this is not in their best interest;
- adversely impact fund investors as accepting cash compensation for a failed buy-in would reduce investment performance and increase cost;
- reduce market efficiency by providing incentives for a counterparty to fail on a trade if they can achieve better terms than settling it; and
- increase trading costs due to risks of monopoly or oligopoly.

ICI Global therefore recommends removing the MBR. If retained, the MBR would force dealers and market makers to consider the potential cost of a mandatory buy-in and would thus result in broker dealers trading less of these securities or adding a premium to the bid-ask spread to offset for the potential cost of a failed trade. It would impact securities lending in a similar way. By harming liquidity, the MBR would increase costs, disadvantage investors, and reduce the EU's competitiveness. The paper recommends that cash penalties

be used to reduce settlement failures.

If the MBR is retained, ICI Global recommends that it is made voluntary, giving the non-failing party the ability to use the buy-in rule if in their best interest. This would provide a guaranteed layer of investor protection and safety in the settlement system and is consistent with international best practices. ICI Global also recommends that the MBR, if retained, is implemented based on a comparison assessment of third-country markets that have introduced it and only as a last resort measure and if it can be demonstrated that mandatory buy-ins will not negatively impact fund investors - including in, but not limited to, stress scenarios.

ICI Global supports the payment symmetry and cash penalties proposals in the REFIT, subject to the following clarifications. Regarding payment symmetry, REFIT should be amended to clarify that in all cases where the price of financial instruments agreed at the time of the trade is different from the price used to determine cash compensation, the corresponding difference shall be paid by the participant benefitting from such price difference to the other participant within the timescales proposed by the Commission. Regarding cash penalties, the REFIT proposals to exclude from the scope of cash penalties instances where settlement fails are caused by factors not attributable to the participants to the transaction or for operations that do not involve two trading parties should be further clarified by the European Securities and Markets Authority (ESMA) to provide certainty to investment funds and other market participants as to how the penalty regime will be applied.

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endnotes

[1] The proposal is available at
<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52022PC0120>.

[2] The REFIT is available at
<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020DC0690>.

[3] ICI Global, Response to European Commission Consultation on CSDR, is available at
<https://www.ici.org/system/files/2021-07/33081a.pdf>.

[4] Joint Trade Association Letters Regarding Implementation of the CSDR Settlement Discipline Regime, is available at
https://www.ici.org/system/files/private/2021-04/21_itr_csd.pdf and
https://www.ici.org/system/files/2021-07/33688a_1.pdf.