

## **ECB/CESR**

By e-mail to:

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### **Re: ESCB/CESR Standards**

#### ***Nordic Custodian Banks ask for a differentiation in Regulation between Securities Depositories and Custodians***

The following Nordic Custodian Banks have jointly reviewed the ESCB/CESR standards and decided to jointly comment on them:

- Den norske Bank
- SEB
- Nordea
- Danske Bank
- Swedbank
- Svenska Handelsbanken

The Nordic Custodian Banks welcomes the initiative and recognize that a unified European regulation is a very important step in order to achieve further necessary consolidation and integration of the European post-trade market, thereby contributing to the objectives set by the European Council.

Although the Nordic Custodian Banks are in Agreement with a substantial number of the Standards, we must express disagreement with three cornerstone areas of the proposed Standards:

#### **A) The Standards subject Custodians operating systemically important systems to the same regulatory standards as infrastructures**

Historically, CSD's have not been entitled to take credit risk due to their core market functionality as a natural monopoly. Banks are thoroughly regulated, and under this regulation, banks have expertise to take on and mitigate risk. This functionality is performed in a highly competitive environment, thereby effectively distributing risk. In the field of post-trade activity, a general description of banks' activities would be that securities are deposited with a CSD and settlement is done in central bank money, thereby distributing a large proportion of risk out of the system. CSD's are generally allowed only to take minimal risk in this area. A possible explanation for the seemingly unnecessary inclusion of Custody banks under the Standards can be that ESCB/CESR has equated so called ICSD's and CSD's. An ICSD is merging its commercial bank activities with national CSD activities. These mixed entities are a combination of banks and CSD's and as such have difficulties in assessing credits, they are forced to deposit in commercial banks for some of their activity and they conduct settlement in central bank- as well as in commercial bank money. The need for such mixed functions to fully collateralize is fairly clear and it should indeed be reflected also in the Standards for the future.

#### **B) The introduction of the Standards will subject Custodians to several areas of double regulation, without adding extra comfort in addition to existing and coming regulatory environment**

The commercial activities of Custodians, among them the function of extending credit, is already very stringently regulated i.e in Basel I and later in Basel II. The introduction of the Standards to also embrace Custodian banks would enforce yet another set of regulations on the Custodian banks without introducing any new safeguards. This would have a compliance, as well as a cost impact and it is our opinion that this would not be in the best interest of the overall objectives for Europe.

### **C) The risk of distortion of competition and increased financial risks**

If present infrastructure, i.e. CSD's, and intermediaries, i.e. Custodian banks, are regulated in a way leading to the confusion of roles, there is a potential risk of distortion of competition. This is due to the fact that CSD's have certain privileges that are not available to the present intermediaries; Custodian banks. According to the fourth objective set up by the Group, the Standards should promote the competitiveness of European markets by fostering efficient structures and marketled responses to developments. In allowing CSD's the granting of credit, acting as principal on securities lending and developing value added services also lies the obvious potential of a concentration of financial risks.

In Standard 6, ESCB/CESR states: "CSD's should avoid taking risks, to the greatest practicable extent". This stipulation is contradicted in many of the Standards we are objecting against, where the Standards if introduced, indeed would increase the risk exposure of the CSD's.

Based on the above, and especially what is said in A), we would urge the regulators to take Standard 9 out completely, alternatively limit this Standard to make it effective only for CSD's.

The Nordic Custodian Banks have no material objections to the following Standards: 1,2,3,4,7,8,12,16 and 19

There are a few standards that in our opinion definitely should be self-regulating, these are: 13 and 15. For Standard 14 and 17, the principle of self regulation should rule. Under no condition can we find reason to make public; pricing, client specific agreements, information or function descriptions that are commercial and necessary to uphold a competitive environment. For Standard 14, we would urge the regulators to preserve the right for any commercial actor to choose its own customers. For a CSD, that performs an activity of public general interest this should not be an option. Standard 5 might also fit in this category. Our opinion is that current prudent governance of Securities Lending activities is sufficient. By making a CSD principal in the proposed centralized environment, there will be an added element of risk with the CSD – this risk is now under most regulations assumed by the banks in a distributed model.

Standard 10,11 and 18 are three very clear examples of Standards that would be subject to dual regulation and where the 'home passport principle' should rule. It is our opinion that those three Standards are equally or better covered in current banking regulations and if introduced should not embrace Custodians at all.

We would be pleased to talk to you on the phone or to meet with you to go into further detail on this issue, at your best convenience, and in the meantime remain at your entire disposal for any information. Please feel free to contact the appropriate representatives in the below list

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Very Truly Yours,