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sent by e-mail

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Remarks on the T2S URD from the Swiss National User Group

Dear Mr Godeffroy

The Swiss National User Group (SNUG)¹ welcomes the opportunity to comment on the Target2-Securities User Requirements Document.

Switzerland being a major financial centre in Europe with a significant cross-border business has a great interest in harmonisation and in the elimination of currently existing barriers. Our infrastructures and the market participants are keen supporters of the European Code of Conduct on Clearing and Settlement, and we are active participants in European working groups dealing with harmonisation and with the elimination of the Giovannini barriers.

We welcome all initiatives that contribute to the integration of the markets. We attach great potential to T2S in this respect, and we expect great benefits from the participation of our CSD as a member. The CSD is already today acting as an investor CSD for the Swiss banks and for some European banks and has links to all European markets.

We are pleased with the quality of the URD. It is well structured, of a high quality and consistent. In general, processes are accurately described and provide a very valuable description of the proposed domestic and cross-border settlement processes in Europe. In addition to our detailed comments, please find in this letter a summary of issues we would like to draw to your attention.

¹ Members of the Swiss National User Group: Hans Däppen, SIS (Chair); Martin Trüb, SIS; Martina Glaser, Daniel Wettstein, SNB; Gerd Hahn, Peter Lippuner, Matthais Meier, Manfred Stöpper, Credit Suisse; Peter Lorenz, Florentin Soliva, Urs Stähli, UBS AG

Direct connectivity

In a project like T2S it is essential to have simple and clear-cut demarcations between the services that the various providers (T2S and the CSDs) offer. In T2S without direct connectivity this is the case. In T2S with direct connectivity the demarcation gets blurred, because the CSDs' pre-settlement services are partly replicated in or out-sourced to T2S.

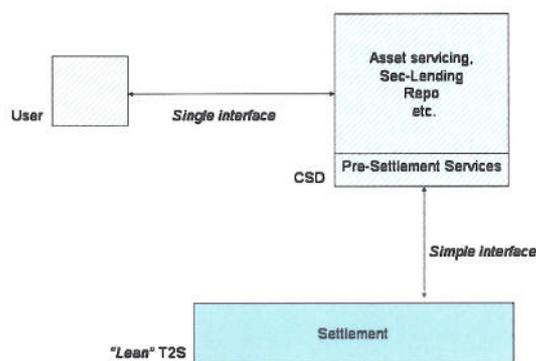


Fig. 1, T2S without direct connectivity

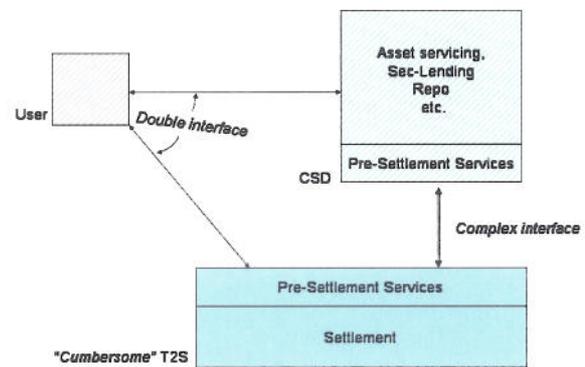


Fig. 2, T2S with direct connectivity

Due to direct connectivity T2S needs a number of additional services:

- T2S needs a process for the acceptance of user instructions (with authentication mechanism etc.)
- T2S needs processes for CSD specific validations
- T2S needs CSD specific algorithms that decide whether the CoSD mechanism has to be activated for a given instruction
- T2S needs CSD specific algorithms that decide whether an instruction has to be pushed to the CSD for processes that are not available in T2S (e.g. tax calculations)
- T2S needs an algorithm that decides whether an instruction has to be pushed to the CSD for the generation of a market claim
- For all CSD specific processes CSDs have to pass corresponding static parameters to T2S
- T2S needs a matching facility (more on matching below)
- Users still need an interface to every CSD in which they are member

T2S Principle 3 would provide for the simple and clear-cut demarcation that we consider necessary for T2S. Principle 3 states that "T2S will serve only as a technical plat-

form for providing settlement services to CSDs". A strict observance of this Principle would altogether exclude the offering of direct connectivity, and it would thus keep T2S as lean as possible.

Direct connectivity is not a must for the majority of the CSD users and its benefits are limited to a small number of large players. This means that the total additional costs between the "lean" T2S of Figure 1 and the "cumbersome" T2S of Figure 2 should be borne by those who wish to use direct connectivity.

Matching processes

We prefer a solution where matching and settlement are unbundled and have separate tariffs and cost accounting. Market forces can then decide on the best matching location (CSD or T2S).

The proposed solution with a user's choice is presumably an attempt to achieve the above. However, the choice to match at the CSD is not a real choice as the place of matching will finally depend on the location, connectivity and matching choice of the counterparty. On the other hand, the choice to match in T2S will always be fulfilled. The playing field is in other words so uneven that hardly anybody would opt for matching in the CSD.

Therefore, we suggest two options how matching could take place in T2S:

1. A straight forward and efficient option would be to match all instructions in T2S. Nevertheless, this solution would not let the market forces come into play.
2. An option which would offer matching in a competitive way on a level playing field is when the choice of matching is with the individual CSDs instead of the individual users. CSDs should be able to decide, based on their own costs and on the T2S tariffs, whether to outsource matching or not. Every CSD is able to carry out matching - notably for both, domestic and cross-CSD settlements². CSDs that do not outsource will therefore match all their domestic instructions and all cross-CSD instructions for which they are the last CSD in the settlement chain. Instructions from direct connectivity would also be matched in the CSD. The only exception would be instructions where both parties use direct input. The solution with a choice for the CSDs does not involve any costs for T2S: CSDs are just other entities (like exchanges and CCPs) that submit already matched instructions to T2S. It does also not have cost implications for the CSDs: if they want to settle cross-CSD transactions in T2S they need links to other CSDs for cross-CSD asset servicing, and through these links they will submit their cross-CSD instructions for matching.

² In cross-CSD situations - no matter how complex the chain of Investor CSDs, technical Issuer CSDs and Issuer CSD may be - matching would take place in the last CSD of the chain. This CSD is identifiable at all times: otherwise the realignment mechanism in T2S would not work.

Furthermore, we would like to point out that regardless whether the users may have the choice for matching location between the CSD and T2S or not and which approach might be the better one, matching itself is by definition not a component of the settlement process. Therefore we suggest that T2S makes a clear demarcation between matching and settlement and that the prices for both services are unbundled.

Settlement timetable

The timetable does not sufficiently take into account the corporate actions processes that have to be carried out by the CSDs. The time span between the "End of Day Reporting" and "New validations on the instructions received" is too short in order to finish the corporate action processes within the CSDs. According to the standards for the elimination of the Giovannini Barriers, payments (cash and securities) should be executed as early as possible on the pay date and the pay date should be one business day after the record date. This means that CSDs have to do all calculations and corporate actions instruction generation after the "End of Day Reporting" (on record date) and before the "New validations on the instructions received" (pay date). The time in the current timetable is almost certainly too short for that.

Furthermore, we do not see why the change of settlement date has to be so early in the day. This creates inconveniences for those active in the US markets, because the US markets still operate with the old settlement date. Similarly it is not clear to us why daytime settlement starts so early in the day. In our opinion daytime settlement only makes sense when new liquidity can be transferred from T2 into T2S, i.e. after 07:00. For all the above reasons, we would prefer a timetable with roughly the following benchmarks:

End of Day Reporting:	18:45
Maintenance Window:	18:45-23:00
Change of settlement date:	23:00
New validations of the Instructions etc:	23:15-24:00
Night-time settlement:	24:00-07:00

This timetable provides sufficient time for corporate action processing (from 18:45 to 23:00) and it avoids the early change of settlement date.

Corporate Actions

We foresee corporate action processing remaining with the CSDs and not becoming a part of T2S functionality. Consequently, we support a differentiation between corporate actions and settlement processes and therefore want a clear separation of the pricing for corporate actions bookings and settlement. In some countries corporate actions bookings are free of charge (e.g. Switzerland). We propose that this issue is considered and outlined in the Economic Impact Analysis.

Please do not hesitate to contact us if you have any questions. We look forward to further discussions with you on these topics.

Swiss National User Group



Hans Däppen
Chairman

Annexes:

- Details URD, public part
- Details URD, confidential part
- Details Economic Impact Analysis
- Answer to additional questions T2S Info Meeting 22.1.08