

## Summary note

# Impact analysis report - non-compliance with T2S harmonisation standards version 2.0

*This summary note updates the T2S Advisory Group (AG), in view of its reporting to the T2S Board, on T2S markets' non-compliance with T2S harmonisation standards. The detailed analysis can be found in the report entitled "Impact Analysis Report - non-compliance with T2S harmonisation standards" (version 2.0), which is attached to this summary note. Compared with the initial version of the impact analysis, it includes the proposed implementation plan of the German market and reports on the on-going monitoring of the implementation plans of the five T2S markets already covered in report.*

## 1. Background

The T2S Board, based on the input received from the T2S Advisory Group (AG), published on 10 December 2013 its [View on the T2S harmonisation standards compliance framework](#) (the T2S Board View).<sup>1</sup>

In the same publication, the T2S Board invites the AG to analyse, on a case-by-case basis, the externalities of a particular T2S market's non-compliance with the T2S harmonisation standards on the T2S community as a whole, and to advise the T2S Board on the course of action to be taken. This impact analysis is to be carried out whenever the respective T2S National User

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<sup>1</sup>

[http://www.ecb.europa.eu/paym/t2s/pdf/View\\_of\\_the\\_T2S\\_Board\\_on\\_the\\_T2S\\_harmonisation\\_standards\\_compliance\\_framework.pdf?ccdface5ac02badcfedbf05b6e44e7a1](http://www.ecb.europa.eu/paym/t2s/pdf/View_of_the_T2S_Board_on_the_T2S_harmonisation_standards_compliance_framework.pdf?ccdface5ac02badcfedbf05b6e44e7a1)

Group (NUG) notifies the AG that it is unlikely for the respective T2S market to comply with one or several T2S harmonisation standards by the migration date of the relevant CSD to T2S.

The T2S Board View also includes a number of potential measures that the AG could consider when formulating its advice on the course of action to be taken:

1. Ex ante measures
  - raise awareness of the impact analysis results to the non-compliant market;
  - escalate bilaterally with the relevant actors in the non-compliant market;
  - escalate the matter to the Governing Council of the ECB.
2. Ex-post measures:
  - postponing the deadline for compliance of the T2S market in question, if there is satisfactory evidence that the T2S harmonisation standard(s) will be met;
  - (the AG) to consider measures of limiting the asymmetry of non-compliance with the complying T2S markets;
  - consider the postponement of the migration date of the relevant CSD, provided that non-compliance makes migration impossible from a technical and legal perspective.

By 27 November 2014, six T2S NUGs (Switzerland, Germany, Romania, France, Belgium, Netherlands) declared that it was *unlikely that their markets would fully comply with some of the mandatory T2S harmonisation standards by the time their markets plan to migrate to T2S*. For five of these non-compliance T2S markets, the T2S Board had already taken decisions in December 2014. The implementation plan of the German market, which was not available in November 2014 when the initial version of the impact analysis was approved by the T2S AG, is now part of the non-compliance impact analysis v.2.0. No new cases of non-compliance have been identified by 17 February 2015.

***Section 2 summarises the detailed non-compliance impact analysis and details the AG proposals on potential measures the T2S Board could consider taking.***

***Section 3 summarises the AG proposals, set out in Section 2, for the T2S Board's consideration.***

## **2. Results of the non-compliance impact analysis**

The impact analysis includes the following non-compliance cases: **Switzerland** for the standard on the Schedule of the T2S settlement day and **Germany, France, Belgium, Netherlands** and **Romania** for the T2S corporate actions standards.

## 2.1 Switzerland

Table 1: Swiss market impact (Migration wave 1, 22 June 2015)

<b><u>CH non-compliance: T2S Settlement Schedule</u></b>	
<b>Overall impact</b>	<b>LOW</b>
<i>Severity (qualitative)</i>	<i>LOW</i>
<i>Expected volume/frequency (quantitative)</i>	<i>LOW</i>
<i>Risk of not achieving full compliance</i>	<i>LOW</i>

The Swiss market will not fully comply with the Schedule of the T2S Settlement Day by its migration to T2S. Non-compliance will affect the sequences for processing corporate actions (CAs) on stock and on flow during night-time settlement. According to the implementation plan, compliance will only be achieved at the beginning of migration wave 2, i.e. March 2016.

Non-compliance will result in a delay in the processing of corporate actions (CA) by SIX SIS on securities and cash accounts of its participants in T2S. As a consequence, availability of cash liquidity to the Swiss CSD (SIX SIS) participants will be delayed. The AG assessed that this is not problematic due to the low volumes at stake. Based on the figures provided by the Swiss NUG, there are currently 358,000 transactions processed in euro annually affecting 540 ISINs. In addition, there are approximately 18,040 CA transactions in euro related to those ISINs. Most of these CA transactions are cash distributions and market claims on such cash distributions which do not affect the underlying security/ISIN. Only around 200 transactions (i.e. 20 CA events, with roughly 10 CA transactions per event) result in a change of ISIN which will also be affected by this non-compliance case. In T2S, it will only be possible to process these CA transactions with a delay of approximately 4.5 hours due to the Swiss markets non-compliance with the related T2S harmonisation standard.

Non-compliance of the Swiss market will also result in the temporary unavailability of certain ISINs and the restrictions that SIX SIS has to impose on their processing prior to the completion of CA events (e.g. partial redemption and new issuance). When SIX SIS is the Issuer CSD, Investor CSDs will need to temporarily restrict settlement with such ISINs until the processing of the CAs will have been finalised. The AG assessed that this is manageable by raising awareness with a view to achieving compliance by March 2016.

### **December 2014 T2S Board decision**

Given the low impact, low volume and the low risk of non-compliance by wave 2, the T2S Board decided to:

- raise awareness of the impact analysis results to the Swiss market;
- monitor (via the ECB team) the implementation plan of the Swiss market.

### **ECB team monitoring results**

The Swiss NUG has confirmed that the analysis and design phase was concluded in January 2015 (in line with the implementation plan).

### **AG advice to the T2S Board**

The AG invites the T2S Board to take note that based on the confirmation received by the Swiss NUG, the Swiss market is progressing with the implementation of its compliance plan as scheduled. No further measures are proposed by the AG.

## **2.2 Germany**

Table 2: German market Impact (Migration wave 3, September 2016)

<b><u>DE non-compliance: T2S corporate actions standards</u></b>	
<b>Overall impact</b>	<b>HIGH</b>
<i>Severity (qualitative)</i>	<i>HIGH</i>
<i>Expected volume/frequency (quantitative)</i>	<i>MEDIUM</i>
<i>Risk of not achieving full compliance</i>	<i>HIGH</i>

The German market will not fully comply with the T2S CA standards by its migration to T2S.

Since the December 2014 T2S Board meeting, Clearstream (CBF), on behalf of the German NUG, has provided a very detailed implementation plan with the aim to achieve compliance with most standards within six months after its migration to T2S. The key elements of this plan can be summarised as follows:

1. A record date rule will be introduced on 1 January 2016, i.e. prior to Clearstream's migration to T2S in September 2016.
2. Further CA standards (market claims standards no. 9, 10, 11, 14, 15 and transformation standard no. 11) will be implemented within six months of CBF's migration to T2S. These refer to management of cash entitlements related to market claims and management of securities fractions.
3. For the remaining CA standards to be implemented (market claims standards no. 7 and 19), the German market has not announced a concrete implementation date yet. Gaps refer to the "CUM" indicator in the T2S messages and the generation of market claims only after the underlying transaction has settled. Implementation is either dependant on the consent of German public authorities or agreement in the German Market Practice Committee.

The AG welcomes the envisaged introduction of a Record Date in the German market custody framework prior to Clearstream's migration to T2S. This should contribute to the alignment of the German market with the market standards for processing CAs as well as the T2S CA standards. CBF estimates the affected settlement instructions related to German ISINs which

have to be managed outside the harmonised framework to be between 1,000 and 10,000 settlement instructions per year, which, according to the agreed AG impact analysis methodology, is being assessed as having a medium impact with regards to the expected settlement volumes for this time period. However, the six-month delay in complying with some important CA standards will result, for this period, in a high impact on the rest of the T2S community.

The AG takes note that, according to the German market estimations, after the six months period after CBF migration to T2S, when the level of compliance is increased, the affected volumes are expected to drop drastically. CBF and the German NUG have committed to monitor closely the affected volumes and report the numbers to the ECB team as soon as data are available.

Based on the information provided and the German implementation plan, the AG has concluded that, although the German market's initial non-compliance will have a high impact overall, it can be reasonably expected that this impact, both qualitative as well as quantitative, will become low at the latest six months after CBF will have migrated to T2S.

#### **December 2014 T2S Board decision**

The AG was not in a position to finalise the impact analysis of the German market for the T2S Board meeting in December 2014; so the substance discussion on the impact of the German market non-compliance with some T2S CA standards was postponed for the next version of the impact analysis of the AG.

#### **ECB team monitoring results**

The ECB team will start monitoring the German market implementation plan once the T2S Board provides its view based on the AG advice.

#### **AG advice to the T2S Board**

Given the information provided by the German market, including its implementation plan, to take note that there will be a high impact of the German market non-compliance to the rest of the T2S Community for a maximum period of six months after CBF's migration to T2S. This impact is expected to be low thereafter.

Based on that, the T2S Board is invited to

- raise awareness of the impact analysis results to the German market;
- monitor (via the ECB team) very closely the implementation of the compliance plan of the German market.

- ask the German NUG to provide as soon as possible to the ECB Team the relevant statistics on the settlement volumes which still will be affected by the non-compliance after the six months period

## 2.3 Romania

Table 3: Romanian market impact (migration wave 1, June 2015)

<b>RO non-compliance: T2S corporate actions standards</b>	
<b>Overall impact</b>	<b>MEDIUM</b>
<i>Severity (qualitative)</i>	<i>HIGH</i>
<i>Expected volume/frequency (quantitative)</i>	<i>LOW</i>
<i>Risk of not achieving full compliance</i>	<i>MEDIUM</i>

The Romanian (RO) market, and Depozitarul Central (DC) when acting as **issuer CSD**, will not raise market claims and transformations in accordance with the T2S CA standards. In effect, market claims and transformations will not be generated at all by Depozitarul Central as of its migration to T2S (June 2015).

As a consequence, investor CSDs connected to DC, will have to decide on what type of CA transaction management service they wish to provide to their participants or alternatively leave it to them to manage bilaterally with their counterparties market claims and transformations on RO ISINs.

When in its **investor CSD** role, DC will generate CAs on flows according to the T2S CA standards. No negative impact is identified for DC participants and other investor CSDs.

DC non-compliance as issuer CSD will have a high impact from competition perspective as this set-up results in a non-level playing field for the foreign entities connected to DC (investor CSDs and market participants); the lack of harmonisation of the processing of the CAs on flow for those RO-ISINs creates in effect a barrier to access the Romanian securities, while on the other hand, Romanian market participants can freely access all other ISINs in T2S (assuming that other T2S markets progress with their harmonisation plans).

Frequency is expected to be relatively low due to:

- First, the very limited number of securities transactions in RO ISINs to be settled on T2S. This is due to the low settlement volumes as well as to the set-up of the migration of DC to T2S, where initially the majority of securities settlement will stay in the books of DC.
- Second, the technical limitation to settle only CA securities entitlements on RO ISINs in T2S (since RON cash entitlements will be settled outside T2S);

The Romanian market provided a detailed plan for full compliance on 31 October 2014 to the AG Chairman. According to the plan it will achieve full compliance no later than February 2017.

#### **December 2014 T2S Board decision**

Given the expected low volumes and the related low impact on T2S markets, the T2S Board decided to:

- raise awareness of the impact analysis results to the Romanian market;
- monitor (via the ECB team) the implementation plan of the Romanian market.

#### **ECB team monitoring results**

According to the information received from the Romanian NUG:

1. The Romanian Market Implementation Group (MIG) sent in December 2014 to the Romanian Financial Supervisory Authority (FSA) the proposal for the amendments to the secondary legislation considered as needed for corporate action standards implementation. These are currently under FSA's analysis and the Romanian MIG is waiting for the feedback.
2. The Romanian Capital Markets Law was amended in January 2015 with respect to corporate actions settlement and now it stipulates that the cash proceeds have to be paid through the CSD and its participants.
3. The solution for settlement of cash proceeds from corporate actions in RON on the same NCB cash accounts, which are used for settlement of transactions by DC participants, has been agreed between DC and National Bank of Romania. DC is now analysing the amendments that should be done to its current agreement with National Bank of Romania to reflect this.

#### **AG advice to the T2S Board**

The AG invites the T2S Board to take note that the Romanian market is progressing with the implementation of its compliance plan as scheduled. No further measures are proposed by the AG.

## **2.4 ESES markets**

Table 4: ESES markets impact (migration wave 2, March 2016)

<b>FR, BE and NL non-compliance: T2S corporate actions standards</b>	
<b>Overall impact</b>	<b>MEDIUM</b>
<i>Severity (qualitative)</i>	<i>MEDIUM</i>
<i>Expected volume/frequency (quantitative)</i>	<i>MEDIUM</i>
<i>Risk of not achieving full compliance</i>	<i>LOW</i>

The ESES markets (FR, BE and NL) confirmed that they will not be able to fully comply with the T2S CA Standards on transformations, for some corporate events, by the time of their migration to T2S in March 2016. The reason behind this implementation gap is the ESES' markets non-compliance with the underlying EU market standards<sup>2</sup> for elective CAs. The plan is for ESES markets to fully comply with these, as well as the T2S CA standards, by September 2016.

The non-compliance of the ESES markets affects the management of transformations and buyer protection on elective CA events such as distributions with options (e.g. optional dividends) or voluntary reorganisations (e.g. tender offers). In particular, transformations on elective CAs either will not be generated at all or, if generated, this will not be done in accordance with the EU and T2S CA Standards (independently of whether or not the affected ISINs are issued in ESES markets). As a consequence participants in investor CSDs, linked to ESES CSDs, will also not be able to process elective events (connected to transformations and buyer protection) according to the T2S CA standards.

Medium impact (severity) is expected for CSDs in T2S and their participants, which have to support non-standard and possibly manual processing for managing these transactions on a regular basis, independently of the location of issuance of the affected ISIN.

In terms of volumes, there is a limited share of the affected CA elective events, basically mandatory reorganisations with options and voluntary reorganisations. Based on past annual average figures provided by Euroclear, these events represent:

- 1.3% of the total volume of CA events on FR ISINs processed by Euroclear FR.
- 3.6% of the total volume of CA events on BE ISINs processed by Euroclear BE
- 0.5% of the total volume of CA events on NL ISINs processed by Euroclear NL

Based on historical figures, there are altogether 1,372 CA elective events within the ESES CSDs per year for which they were the Issuer CSDs. There are no volume estimations on the number of affected settlement instructions. However, the elective CAs on non-ESES ISINs would also have to be taken into account for settlement involving participants of Euroclear ESES CSDs.

#### **December 2014 T2S Board decision**

Given the expected medium size volumes and the low risk of non-compliance continuing through September 2016, the T2S Board decided to:

- raise awareness of the impact analysis results to the ESES markets;
- monitor (via the ECB team) the implementation plan of the ESES markets.

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<sup>2</sup> Corporate Actions Joint Working Group (CAJWG) standards



### **ECB team monitoring results**

Monitoring was done as part of the CASG gap analysis for 2015. Euroclear's representative informed the CASG that the original plan of achieving full compliance with T2S CA standards by September 2016 is still valid. There are no barriers to full implementation by the agreed timeline.

### **AG advice to the T2S Board**

The AG invites the T2S Board to take note that the ESES markets are progressing with the implementation of their compliance plans as scheduled. No further measures are proposed by the AG.

## **3. Conclusions**

The AG invites the T2S Board to consider the following points:

### ***Switzerland***

To take note that, based on the confirmation received by the Swiss NUG, the Swiss market is progressing with the implementation of its compliance plan as scheduled.

### ***Germany***

Given the information provided by the German market, including its implementation plan, to take note that there will be a high impact of the German market non-compliance to the rest of the T2S Community for a maximum period of six months after CBF's migration to T2S. This impact is expected to be low thereafter.

Based on that, the T2S Board is invited to:

- raise awareness of the impact analysis results to the German market;
- monitor (via the ECB team) very closely the implementation of the compliance plan of the German market;
- ask the German NUG to provide as soon as possible to the ECB Team the relevant statistics on the settlement volumes which still will be affected after the six months period.

### ***Romania***

To take note that the implementation of the compliance plan of the Romanian market is progressing as scheduled.

### ***ESES***

To take note that the ESES markets are progressing with the implementation of their compliance plans as scheduled.